

Exhibit I

In The Matter Of:

*UNITED STATES OF AMERICA v.
MARIO S. LEVIS A/K/A SAMMY LEVIS*

*VOLUME 9
April 8, 2010*

*TRIAL
SOUTHERN DISTRICT REPORTERS
500 PEARL STREET
NEW YORK., NY 10007
212-805-0300*

Original File 048WLEVF.txt, Pages 1298-1464 (167)

Word Index included with this Min-U-Script®

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THE COURT: Received.

(Government Exhibit 1206 received in evidence)

BY MR. STELLMACH:

Q. If we could go, Mr. Cunningham, to your e-mail that starts the chain on Page 3, the e-mail dated February 10th that you sent to Mr. Levis, and if we could just highlight the final paragraph beginning "Finally."

Would you please read that for us.

A. Sure. "Finally, while you have said that the typical rate you pay is LIBOR plus 150, it is my understanding that some of the loans you have sold have no caps in place. Therefore, there is certainly the possibility that Doral could be underwater on some of these at some point in the future. Can you quantify the amount that do not have caps?"

Q. What was your basis for saying that it was your understanding that some of the loans did not have caps?

A. Right, I had spoken with other institutions and other people in Puerto Rico regarding these loan sales.

Q. Do you recall speaking about these loan sales with anyone from Western Bank, including an individual named Freddie Maldonado?

A. Yes.

Q. What do you recall from those conversations?

A. I had asked Western Bank if they had any of these instruments, and if they did or if they didn't, if they were

getting the idea that some have no caps? That is not true at all. Maybe you are referring to the fixed IOs which don't need caps since they are fixed. These caps are embedded in each contract and all of them are significantly below the WAC of the loans, so Doral will always have a hefty and positive spread.

"Also it's important to note that most existing net yields paid to investors are close to the caps. The pricing ranges from LIBOR plus 100 to 150, probably for an average of 125. Hope this helps, regards, Sammy."

THE COURT: Just one minute.

MR. STELLMACH: Sorry, your Honor?

THE COURT: I just would like to read this.

(Pause).

THE COURT: Go ahead.

MR. STELLMACH: Yes, your Honor.

BY MR. STELLMACH:

Q. Prior to receiving this e-mail, Mr. Cunningham, had defendant ever mentioned contractual caps to you before?

A. No.

Q. What did you understand when he wrote that the caps were embedded in the contracts?

Did you understand that to be referring to a particular type of cap?

A. Just that caps were, indeed, part of the contracts.

Q. What did you understand when he wrote that the caps were

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aware of the existence of any caps. I believe then that they did -- whether they had them or not, I do believe they did own some of these and they said that they did not have caps within the contracts.

Q. And so what were you trying to communicate when you said there was a possibility that Doral could be underwater on some of the contracts at some point in the future?

A. Well, right. If Doral is receiving X and having to pay out some lower rate at least at this given time, but that lower rate then is variable, then feasibly there is no, there is no protection. At some point they could be paying -- if they're receiving 10, hypothetically they could be paying 20 percent, 30 percent, 40 percent. These are gross numbers, but that is the point. They would be underwater paying out far more than they're receiving.

Q. By "underwater," you just meant the pass-through rate Doral is paying could be higher?

A. Correct.

Q. Than what it is received on the coupon from the borrower?

A. Correct.

Q. Could we go to Mr. Levis' response on the same date, February 10th of 2005. If you could blow that up and highlight the section beginning with regarding caps. Could you read that for us, Mr. Cunningham.

A. "Regarding caps, all loans sold have a cap. Where are you

significantly below the WAC of the loans?

A. That the WAC then would be the rate that the underlying was paying, and then the cap then would be below that so that there would, indeed, be a spread that Doral would be able to realize.

Q. So that --

A. A minimum spread in the worst case, if you want.

THE COURT: Just keep your voice up.

THE WITNESS: Yes.

THE COURT: What did you just say?

THE WITNESS: Can you repeat?

BY MR. STELLMACH:

Q. I was asking Mr. Cunningham what you understood the defendant to mean when he wrote that the caps were significantly below the WAC of the loans?

A. So the WAC then is a weighted average coupon that is being received by Doral. The cap then presumably, as he stated, is below that rate that they received. So, therefore, should be some positive spread maintained because of the existence of that cap.

THE COURT: Positive spread, the money that Doral can keep?

THE WITNESS: That's correct.

THE COURT: Okay.

BY MR. STELLMACH:

Q. In fact, it is described as a hefty and positive spread,

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[1] right?

[2] A. Yes, yes.

[3] Q. What did you understand the defendant to mean when he wrote
[4] most existing net yields paid to investors are close to the
[5] caps?[6] A. (A) That the yield that the investors are receiving
[7] currently, that whatever the time of this was would not go any
[8] higher. Therefore, all else equaled, any further increase in
[9] LIBOR would not negatively affect Doral, no further impairments
[10] all else equal.[11] Q. Now, there are financial hedging instruments that Doral
[12] could have purchased that would have made money as interest
[13] rates went up. Is that right?

[14] A. Correct.

[15] Q. Is there a difference between a cap that's contained in a
[16] sales contract versus a hedge you can buy in the market?[17] A. Well, certainly. The cap again is within the contract.
[18] Assuming the contract is upheld and both parties know the
[19] absolute interest rate or the reference rate at which point the
[20] receiving party won't get more, Doral won't pay out more than
[21] that.[22] The hedge then has nothing to do with the IO or the cap.
[23] It is a total separate instrument. Really they don't relate to
[24] each other at all except that hopefully the hedge then will
[25] offset what's going on with the value of the IO.[11] asked when the K, the 10K would be out. Near the end of the
[12] month in February? No, probably early March. New disclosure,
[13] that's what people are looking for in essence.[14] Q. If you go to Page 1, which is one of your responses, if you
[15] blow up the first paragraph, this is also February 10th, can
[16] you walk us through those first few sentences.

[17] A. You mean read it or summarize?

[18] Q. If you want to read it and then summarize, that is fine or
[19] if you just want to read it.[10] A. (Pause) I am going through here with Mr. Levis that, Sammy
[11] Levis, that, indeed, more disclosure, meaning more information
[12] than their 10K would be very helpful. There are a lot of
[13] question marks in the marketplace over the valuations assigned
[14] specifically to the IO.[15] Think like an investor, give what you would want --
[16] you being Mr. Levis -- as an investor and then more, basically
[17] the crux of that paragraph there.[18] Q. You write about wanting more clarity on gain on sale
[19] margin, the valuation of the IO and hedging. Do you recall
[20] what questions you had about hedging at this point?

[21] A. Not specifically, no.

[22] Q. If you go to Government Exhibit 1207, I'll ask you whether
[23] you recognize that document?

[24] A. Yes, another e-mail correspondence.

[25] Q. With?

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[1] Q. We'll come back to that point later.

[2] From your perspective, in evaluating Doral and making
[3] recommendations for investors, is there any difference in the
[4] comfort that you take from a contractual cap versus a hedge you
[5] can buy in the marketplace?[6] A. Yes. Again the contractual cap, and assuming everyone
[7] upholds both sides, as I said, the cap -- you're going to know
[8] with absolute certainty what Doral would be paying out.[9] The hedge, on the other hand -- (A) it is not clear what it
[10] is. There is a multitude of different hedging instruments, and
[11] you have absolute behavior, it isn't an absolute is probably
[12] the best way to say that. Hedges can behave very differently
[13] in different interest rates. That is what we are talking about
[14] here, different interest rate environments.

[15] THE COURT: Go ahead.

[16] MR. STELLMACH: Yes, your Honor.

[17] BY MR. STELLMACH:

[18] Q. If you turn to page -- we are still on Page 2 -- if you go
[19] further up to an e-mail that the defendant sends you at 1:12 on
[20] February 10th, can you explain to us -- I am sorry. I think we
[21] were still on Page 2. It is the e-mail from Mr. Levis,
[22] dated -- that's it. Thank you.[23] Can you explain to us what's reflected in that exchange
[24] with Mr. Levis.

[25] A. Oh, right. In the previous e-mail or in the chain I had

[1] A. With Sammy Levis.

[2] MR. STELLMACH: Your Honor, the government offers
[3] Exhibit 1207.

[4] THE COURT: Received.

[5] (Government Exhibit 1207 received in evidence)

[6] BY MR. STELLMACH:

[7] Q. If we go, Mr. Cunningham, to your e-mail that starts on the
[8] bottom of Page 2 and continues on Page 3, if you could walk us
[9] through the concerns you express. You write I have been doing
[10] more work on the IO and I have found the following. It starts
[11] at the bottom of the page.

[12] A. The bottom of 2?

[13] Q. That's right.

[14] A. Okay. Do you want me to read this aloud?

[15] Q. Just walk us through in general terms what your concerns
[16] are.[17] A. Right. So it says I've done more work on the IO. The
[18] estimates that I've found -- there is roughly 6 to 6 and a half
[19] billion in notional balances or mortgages supporting those.[20] Average life is 7 years and note that this could be
[21] consistent with comments that the company has made in the past.[22] Q. I am sorry to interrupt. I was looking at the second to
[23] the last paragraph right where you wrote "I estimate." Could
[24] you read that for us. If you could just highlight that.

[25] A. I am sorry. "I estimate that there could be another 190

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[1] million in impairments on the current portfolio should rates go
[2] past 4.25 percent."

[3] **Q.** After you write that, could you take us through Mr. Levis'
[4] response which is on Page 2. If you can read that for us,
[5] please?

[6] **A.** Sure. I cannot comment much until the 10K is out.
[7] However, your final conclusion that gain on sale margin will
[8] have to be declining may not necessarily be true. First the
[9] gain on sale is determined by the sale of new originations
[10] which already has a higher coupon in nonconforming since we
[11] have already increased the WAC charged to borrowers on new
[12] nonconforming by about 50 basis points.

[13] Bear in mind that these loans have very low balances,
[14] 50 to 60 million, amortized over 30 years. So a change in the
[15] WAC does not affect much the monthly payment the borrower pays.
[16] So in a way these loans are less price sensitive. In other
[17] words, although mortgage rates have not increased much in the
[18] U.S., at our company we already increased the rate offers for
[19] the nonconforming, and so far no impact on originations. The
[20] higher coupon offset the higher LIBOR rate. Secondly, in the
[21] text exempt on the new housing, the premium has not changed at
[22] all because of the local market.

[23] **Q.** Mr. Levis doesn't mention anything about contractual caps
[24] in his response to you, does it?

[25] **A.** No.

[1] margin was likely to be falling. Capital --

[2] **Q.** Sorry to interrupt. What do you mean by gain on sale
[3] margin is falling?

[4] **A.** In recent quarters, to the best that I recall, in recent
[5] quarters a gain on sale margin had been quite high. I think at
[6] times, and this won't be exact, but in the high teens, maybe
[7] near 20 percent.

[8] Historically, if you look over the past many, many years,
[9] the gain on sale margin had been markedly lower. We believe
[10] that was going to be falling.

[11] Then in the third point, we point out that due to the IO,
[12] there is risk here, we don't think the capital, the capital
[13] ratios were strong. There as perhaps some believed and with
[14] the risks that we saw, we had moved to a hold rating and
[15] lowered it, I believe we lowered the target price.

[16] **Q.** What about the representation that had been made to you
[17] about the existence of caps?

[18] At this point what weight are you placing on that
[19] representation?

[20] **A.** I would have to say by going, going to a hold or seeing or
[21] believing that there were more impairments, that I didn't
[22] believe that the -- I didn't believe caps were in existence.

[23] **Q.** If we could just jump back to Government Exhibit 1207 on
[24] Page 3, and I think we can also follow along, Mr. Cunningham,
[25] on the screen, the last two sentences in the first paragraph,

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[1] **Q.** In fact, after Government Exhibit 1206, the e-mail from
[2] February 10th, did Mr. Levis ever raise the issue of
[3] contractual caps with you again?

[4] **A.** I don't believe.

[5] **Q.** If you look at Government Exhibit 1208, do you recognize
[6] that document?

[7] **A.** Yes, I do.

[8] **Q.** How do you recognize it?

[9] **A.** It was a downgrade of the shares that I published.

[10] **Q.** If you could --

[11] **THE COURT:** What is the date?

[12] **MR. STELLMACH:** March 7th, 2005, your Honor. The
[13] government offers Exhibit 1208.

[14] **THE COURT:** Received.

[15] (Government Exhibit 1208 received in evidence)

[16] **BY MR. STELLMACH:**

[17] **Q.** If you see up top, it indicates change in recommendation
[18] right beneath the date at the top, and you downgraded Doral to
[19] a hold. Is that right?

[20] **A.** Correct.

[21] **Q.** Looking at the key points under the section entitled "IO,
[22] IO, down the hold we go," could you just walk us through the
[23] factors that led you to downgrade Doral.

[24] **A.** Sure. The estimates that we had were that future
[25] impairments on the IO were forthcoming, that the gain on sale

[1] if we can have that blown up, and those sentences beginning, "I
[2] estimate that the impairment?"

[3] **A.** Right. "I estimate that" --

[4] **THE COURT:** What exhibit is this?

[5] **MR. STELLMACH:** From the previous exhibit, your Honor,
[6] Government Exhibit 1207, the e-mail exchange that precedes this
[7] report.

[8] **THE COURT:** Whose language is this?

[9] **MR. STELLMACH:** This is an e-mail from Mr. Cunningham
[10] to the defendant.

[11] **THE COURT:** Just a minute. Go ahead with your
[12] questioning, please.

[13] **BY MR. STELLMACH:**

[14] **Q.** Can you read that to us, Mr. Cunningham.

[15] **A.** Yes. "I estimate that the impairment represented a change
[16] in LIBOR assumptions of about 35 basis points. I believe that
[17] the cap on the existing portfolio is, on average, about 4.4
[18] percent. It appears that the impairment was for roughly 600
[19] million in supporting balances."

[20] **Q.** What was your basis for believing that the cap was on
[21] average at 4.4 percent?

[22] **A.** I believed it was a combination then of, combination of
[23] conversations with the company and of our own estimates, and
[24] within that we tried to, as I recall, stratify or go through
[25] each and every quarter of the past many years to see, to

Exhibit J

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*VOLUME 10
April 9, 2010*

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Original File 049WLEVF.txt, Pages 1465-1620 (156)

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[11] Q. Can you describe to the jury why they were part of the
[12] audit plan?

[13] A. They were considered a significant balance to the financial
[14] statements.

[15] THE COURT: They were what?

[16] THE WITNESS: Considered a significant balance, amount
[17] in the financial statements.

[18] BY MR. ANTHONY:

[19] Q. Could you describe what the term "material" means?

[20] A. Material, in simple words is basically what is significant
[21] to the users of the financial or may be significant to the user
[22] of the financial statements.

[23] Q. Is it fair to say that the IOs were a material item in the
[24] company's financial statements?

[25] A. Yes.

[16] MR. ANTHONY: Your Honor, permission to approach.

[17] THE COURT: Sure.

[18] BY MR. ANTHONY:

[19] Q. Mr. Mendez, I'm bringing you a copy of Government Exhibit
[20] 6201. I believe you have an excerpt from this document in your
[21] binder. Mr. Mendez, if you could grab the actual exhibit
[22] there, please, and take a look at it for me.

[23] Do you recognize this document, sir?

[24] A. Yes.

[25] Q. How do you recognize it?

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[11] A. I have seen it before. It's a cover page of a form 10K.

[12] Q. Can you describe for us what that document is?

[13] A. It's a company, Doral Financial's form 10K for the year
[14] ended December 31, 2001.

[15] MR. ANTHONY: Your Honor, at this time, the government
[16] would offer Exhibit 6201 in evidence.

[17] THE COURT: Received.

[18] (Government's Exhibit 6201 received in evidence)

[19] BY MR. ANTHONY:

[20] Q. Mr. Mendez, if you could flip to the first tab in your
[21] document, I believe there should be a excerpt there from the
[22] larger document that you have there, is that correct?

[23] A. Yes.

[24] Q. I'd like to draw your attention to what is the fourth page
[25] of your excerpt. Can you describe for the jury what is
[16] contained on this page?

[17] A. This is a copy of the audit report issued by Price
[18] Waterhouse Coopers for the year ended December 31, '01.

[19] Q. Mr. Mendez, I'd like to draw your attention to a few spots
[20] on here. Do you see in the first sentence, there are items
[21] listed, statements of income, comprehensive income, changes in
[22] stock quotes, equity, and cash flows?

[23] A. Yes.

[24] Q. What are those?

[25] A. It refers to the financial statements that are behind the

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[11] audit report.

[12] Q. Mr. Mendez, do you see down there on the eighth line,
[13] there's a sentence that reads, "These financial statements are
[14] the responsibility of the company's management and our
[15] responsibility is to express an opinion on these financial
[16] statements based on our audits"?

[17] A. Yes.

[18] Q. Could you explain to the jury what that means?

[19] A. The first part of the sentence indicate that management is
[20] responsible for the company's financial statements, the
[21] financials prepared by management, and describes our
[22] responsibility as auditors, which is to express an opinion
[23] based on the work performed in the audit.

[24] Q. Could you read the next line for us, beginning "We
[25] conducted"?

[16] A. "We conducted our audits of these statements in accordance
[17] with auditing standards generally accepted in the United States
[18] of America, which require that we plan and perform the audit to
[19] obtain reasonable assurance whether the financial statements
[20] are free of material misstatement."

[21] Q. Mr. Mendez, can you describe what auditing standards
[22] generally accepted in the United States are?

[23] A. In simple terms, those are the rules that are followed by
[24] the, we follow, followed by the auditors to perform the audits.

[25] Q. And this document says those rules require you to "plan and

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[11] perform the audit to obtain reasonable assurance." Can you
[12] explain to us what reasonable assurance means?

[13] A. Reasonable means that it's not an absolute assurance,
[14] meaning that not all the transactions and balances in the
[15] financial statements are fully tested. They are tested on a
[16] test basis:

[17] Q. And lastly, it reads "about whether the financial
[18] statements are free of material misstatements." Can you
[19] describe for us what material misstatement means?

[20] A. Material misstatement means something that will be
[21] significant to the financial statements that may not be
[22] presented correctly.

[23] Q. I believe the next line reads, "An audit includes examining
[24] on a test basis evidence supporting the amounts and disclosures
[25] in the financial statements, assessing the accounting
[16] principles and significant estimates used by management and
[17] evaluating the overall financial statement presentation." Can
[18] you describe what that sentence is talking about?

[19] A. It has, that's basically a broad description of the work
[20] that auditors perform in the audit, so the first element in
[21] that sentence indicates that it's on a test basis, right, not
[22] everything is tested. And then it describes --

[23] THE COURT: It's a sampling?

[24] THE WITNESS: Sampling, correct.

[25] THE COURT: Not every single transaction of the

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(1) Q. Mr. Mendez, can I draw your attention to page 4 of this
(2) document. Do you see the recommendation that you're referring
(3) to on this page?

(4) A. Yes.

(5) Q. Could you read the recommendation for us, please?

(6) A. "Management should consider obtaining a valuation of the
(7) interest-only strips from an outside source at least once a
(8) year."

(9) Q. And could you read the following paragraph for us also,
(10) please.

(11) A. "Currently, the company values the interest-only strips --"

(12) **THE COURT:** Can it be highlighted again?

(13) A. "Currently the company values the interest-only strips
(14) internally utilizing actual prepayment statistics of the
(15) portfolios. However, we believe that at least once a year, the
(16) interest-only strips should be valued by an outside source to
(17) provide an independent valuation of the portfolio. Given the
(18) high sensitivity of this type of asset to interest
(19) fluctuations, especially in the current downward trend of
(20) interest rates, it is important that the portfolio of
(21) interest-only strips be valued by an expert independent
(22) source."

(23) (Continued on next page)

(24)
(25)

(1) **BY MR. ANTHONY:**

(2) Q. Mr. Mendez, did management, indeed, get another valuation
(3) of the IOs in 2001?

(4) A. Yes.

(5) Q. Where did they obtain that valuation from?

(6) A. Valuation from Morgan Stanley.

(7) Q. Was this the valuation we just referred to when we looked
(8) at the 10K a moment ago?

(9) A. Yes.

(10) Q. Mr. Mendez, I would like to draw your attention now to the
(11) next tab in your binder, Government Exhibit 318. Mr. Mendez,
(12) do you recognize this document?

(13) A. Yes.

(14) Q. What is this document -- sorry -- how do you recognize this
(15) document?

(16) A. It is a typical working paper in the audit file. I
(17) remember it from the audit.

(18) Q. This is from the 2001 audit?

(19) A. Yes.

(20) Q. You were a member of the audit team in that year?

(21) A. Yes.

(22) **MR. ANTHONY:** The government offers Exhibit 318 into
(23) evidence.

(24) **THE COURT:** Received.

(25) (Government Exhibit 318 received in evidence)

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(1) Q. Mr. Mendez, can you describe for us your understanding of
(2) what is meant by the term expert, independent source.

(3) A. My understanding is a competent, objective source of
(4) valuation outside management.

(5) Q. Do you have an understanding of why PWC, the audit team in
(6) Puerto Rico made this recommendation?

(7) A. To my understanding, it was a good practice to obtain an
(8) external valuation for the instruments.

(9) Q. Why is that a good practice?

(10) A. For an area of judgment and for this type of instruments
(11) obtaining external valuations will provide further information
(12) to assess the management estimate.

(13) Q. Is it just one more item to give you reasonable assurance?

(14) A. Yes.

(15) Q. Mr. Mendez, how does management respond to this
(16) recommendation?

(17) A. They obtained an external valuation.

(18) Q. Is this management's response, agree, we expect to have
(19) this independent valuation report during the second half of
(20) 2001?

(21) A. Yes.

(22) **THE COURT:** Are you reading from something now?

(23) **MR. ANTHONY:** Yes, the following page of this exhibit.

(24) **THE COURT:** Can we highlight that.

(25) **MR. ANTHONY:** The top of Page 5.

(1) **THE COURT:** This is from the 2001 audit?

(2) **THE WITNESS:** Yes.

(3) **THE COURT:** Okay.

(4) **BY MR. ANTHONY:**

(5) Q. Mr. Mendez, can you read for us the first line in this
(6) document under the word, "Description."?

(7) A. "The company's policy is to classify IOs as trading
(8) securities. Therefore, securities should be marked to market
(9) with changes in value recorded in earnings. These instruments
(10) are complex and marketability is limited."

(11) Q. Trading securities, is that that category we just looked at
(12) in the 10K?

(13) A. Yes.

(14) Q. Can you describe what marked to market means.

(15) A. Record the balance of the IOs at fair value.

(16) Q. Fair value, is that a term we just defined earlier?

(17) A. Yes.

(18) Q. What does it mean that changes in value are recorded in
(19) earnings?

(20) A. Changes in value are recorded, were recorded in this
(21) statement of income, in this case earnings similar to statement
(22) of income.

(23) Q. The next paragraph, the last line reads, "Currently the
(24) following procedures are performed by management to
(25) obtain/calculate the fair value of the IOs."

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[1] were getting. So that's the actual spread which ranged between
[2] 4, 5, 6 percent.
[3] **MR. ANTHONY:** Your Honor, we may have a more legible
[4] copy.
[5] **THE COURT:** If you take 131 million and you take 3
[6] percent of that, it gives you --
[7] **MR. BLACK:** Your Honor, I think it is 191. It is hard
[8] to read, but that first column says 191.
[9] **THE COURT:** Let's start with 191.
[10] **MR. ANTHONY:** We may have a more legible example we
[11] can use, if that will be okay?
[12] **THE COURT:** We want to get the method. We can
[13] certainly benefit from the figures, too. That is 5.7 million,
[14] roughly. Where do we go from there?
[15] **THE WITNESS:** And then the last factor was 3.884, the
[16] multiple.
[17] **THE COURT:** That was a multiple to sort of estimate
[18] the market value. Is that right?
[19] **THE WITNESS:** Yes.
[20] **THE COURT:** All right. Go ahead, please, go ahead.
[21] **MR. ANTHONY:** Thank your Honor.
[22] **BY MR. ANTHONY:**
[23] **Q.** Mr. Mendez, do you recognize what looks like initials to
[24] the right of this document?
[25] **A.** Yes.

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[1] **Q.** Do you have an understanding of whose initials those are?
[2] **A.** My understanding was Jose Lopez from Morgan Stanley was
[3] signing of those initials.
[4] **Q.** Can you turn to the 5th page of this document.
[5] **A.** Yes.
[6] **Q.** Would you explain for us what is at the bottom of this
[7] document beginning with, "Tota"?
[8] **A.** Would you give me the question again, please.
[9] **Q.** Can you explain for us what is at the bottom of this
[10] document beginning with the total.
[11] **A.** That was the totalization of the IOs aggregate for value.
[12] **Q.** What is this below there? It looks like a signature?
[13] **A.** The signature from Jose Lopez from Morgan Stanley.
[14] **Q.** Mr. Mendez, could you flip back to Government Exhibit 318.
[15] Could you go to the second page at the top. Could you explain
[16] what the section under obtained management's internal
[17] evaluation of the portfolio and tested its mathematical
[18] exceptions meets, what that is referring to?
[19] **A.** It refers that we obtained this constant cash flow model
[20] provided by management and checked the mathematical accuracy,
[21] which is the math of the schedule.
[22] **Q.** I think when we were talking earlier, you also mentioned
[23] that PWC did something additional and came up with some kind of
[24] additional value for the IOs. Can you explain what you meant
[25] by that.

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[1] **A.** Well, we didn't come up with our valuation of the IOs. We
[2] performed an analysis to evaluate the valuation of the IOs as
[3] provided by management. To do that, we evaluated a number of
[4] assumptions to see -- ended up using the evaluation. Then that
[5] is described a little bit later in the working paper from what
[6] I see.
[7] **Q.** Amongst these three, I will refer to them as valuations, I
[8] realize yours was a limited exercise to do something, but
[9] amongst those three, the work the audit team did, the internal
[10] model and Morgan Stanley model, what was your understanding of
[11] which one of those carried the most weight in your audit
[12] evidence?
[13] **THE COURT:** I am sorry. Could you just state the
[14] question again.
[15] **MR. ANTHONY:** Sure.
[16] **BY MR. ANTHONY:**
[17] **Q.** Mr. Mendez, amongst the work the audit team did, the Doral
[18] internal model and the Morgan Stanley valuation, which of those
[19] three carried the most weight as audit evidence at this point
[20] in time?
[21] **A.** The external valuation carries the most weight.
[22] **Q.** Why is that?
[23] **A.** Because an external valuation was considered competent
[24] evidence in assessing the valuation of the instruments.
[25] **Q.** I think you also mentioned earlier that part of your audit

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[1] work during this period was to speak with someone at PWC about
[2] the IO valuations. Is that right?
[3] **A.** Yes.
[4] **Q.** What can you tell us about that exercise?
[5] **A.** We asked someone in the U.S. mortgage banking industry with
[6] experience to provide us with input as to what the company was
[7] doing to value the instruments. So I talked to the people
[8] about it and provided the Excel calculation from management and
[9] the analysis that we were performing to ask for this feedback.
[10] **Q.** Which feedback did you receive from this person?
[11] **A.** He basically described the purpose of the discounted cash
[12] flow model that the company was using served to corroborate
[13] what the company was receiving from Morgan Stanley, that the
[14] mathematical accuracy of present value, of present valuation
[15] declaration was okay, the formula.
[16] He also indicated that management should consider
[17] segregating the portfolio into different characteristics of the
[18] loans, like terms or maturity dates and so forth and the
[19] consideration of the floating versus fixed payments that
[20] investors were getting.
[21] **Q.** Did anyone from the valuation group ever visit Puerto Rico
[22] as part of this exercise?
[23] **A.** No.
[24] **Q.** Did they meet with anyone at Doral?
[25] **A.** No.

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(11) understand further the embedded assumptions that MS uses in its
(12) valuation of the IOs.
(13) **A.** As an indicated area, the company was receiving a valuation
(14) from Morgan Stanley, and we wanted to have the opportunity to
(15) understand further how Morgan Stanley was developing the
(16) valuation.
(17) **Q.** Did you make a recommendation in connection with that
(18) desire, I guess, to better understand what it was Morgan
(19) Stanley was doing?
(20) **A.** Yes, we asked to have a conversation with Morgan Stanley.
(21) **Q.** In this memo do you also make an observation regarding the
(22) internal valuation model?
(23) **A.** Could you repeat the question again, please.
(24) **Q.** Do you also make an observation regarding the internal
(25) valuation model?
May I direct your attention to the section labeled
observations of PWC on DFC's valuation model.
A. Yes, sir. That paragraph refers to recommendations related
to the internal model.
Q. What recommendations is it referring to?
A. The disaggregation of pools of IOs between fixed and
floating pools.
Q. Does that recommendation, does that relate to the
recommendation in the internal control memorandum we just
looked at?

(11) **Q.** How do you recognize this document?
(12) **A.** It is a chain of e-mails in which I participated and I
(13) remember from my period in the audit.
(14) **MR. ANTHONY:** The government now moves for the
(15) admission of Government Exhibit 306.
(16) **THE COURT:** Received.
(17) (Government Exhibit 306 received in evidence)
(18) **THE COURT:** I have a note that you marked for
(19) identification 342. I don't have a note that it is received.
(20) Did you offer it? Did you mean to offer it?
(21) **MR. ANTHONY:** Actually, your Honor, I did not. May I
(22) have that permission?
(23) **THE COURT:** Received.
(24) (Government Exhibit 342 received in evidence)
(25) **BY MR. ANTHONY:**
Q. Mr. Mendez, could you turn to Exhibit 306, your e-mail
dated 7-30-2002 at 3:16 pm. Do you see that?
A. Yes.
Q. Would you explain for us what prompted you to write this
e-mail?
A. It was in response to an e-mail I received from Ricardo
Melendez, where he advised that the company was going to obtain
a second valuation for the IOs on a quarterly basis.
Q. Do you see that e-mail from Ricardo Melendez as part of
this document?

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(11) **A.** Yes.
(12) **Q.** Is it meant to cover both of the points in that memo?
(13) **A.** Yes.
(14) **Q.** Can you remind us what those points were.
(15) **A.** The disaggregation of the pool, pool of loans between the
(16) different, among the different characteristics because the
(17) loans were comprised of different terms and maturities and
(18) interest rates and also between the fixed and floating nature
(19) of the IOs.
(20) **Q.** Can you explain for us what is being discussed under Item
(21) 3, alternatives for the periodic valuation.
(22) **A.** Can you repeat the question again, please.
(23) **Q.** Sure. Mr. Mendez, can you explain for us what is being
(24) discussed under Item 3, alternatives for the periodic valuation
(25) at the bottom of Page 2.
A. This was a recommendation to management to, I guess,
evaluate whether Cohane, an external firm, will be able to
value the IOs, and at that time Doral was using Cohane to value
servicing assets.
Q. Is this a recommendation for Doral to obtain yet another
external valuation?
A. Yes.
Q. Mr. Mendez, would you turn to Government Exhibit 306 in
your binder. Mr. Mendez, do you recognize this document?
A. Yes.

(11) **A.** It is on the next page.
(12) **Q.** 7-30-02 at 8:55 am?
(13) **A.** Yes.
(14) **Q.** Could you translate for us what it is Mr. Melendez writes
(15) to you.
(16) **A.** It says it was decided to obtain two independent valuations
(17) for the IOs on a quarterly basis.
(18) **Q.** Mr. Mendez, turning back to your 7-30-2002 e-mail, could
(19) you explain for us what you're asking in Item 1.
(20) **A.** I was asking who was the second valuation, who was going to
(21) provide the second valuation.
(22) **Q.** The one referred to by Mr. Melendez in the earlier e-mail?
(23) **A.** Yes.
(24) **Q.** Would you explain to us what you're referring to in Item 3.
(25) **A.** It was advising Ricardo Melendez that PWC, the valuation
team, were going to ask for independent confirmation of the
valuations to be provided by external sources.
Q. Can you explain how the independent confirmation process
usually works.
A. It is a process in which the auditors asked for, made a
request to the external source. That letter is signed by
management and provided to us. We mail it to the external
source and we ask them to respond to our request, to request a
repeat to us.
Q. Would you explain to us what is being discussed in Item 5.

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[1] A. It was advising Ricardo Melendez that we wanted to have a
[2] conversation with the sources of the valuation to inquire of
[3] them about their approach and valuation process.
[4] Q. When you say sources of evaluations, what are you referring
[5] to?
[6] A. The two external parties that were going to be providing
[7] the valuation.
[8] Q. So Morgan Stanley is one of them?
[9] A. Morgan Stanley was one of them, yes.
[10] Q. The second would be an unidentified second broker?
[11] A. Yes.
[12] Q. How about Item 7?
[13] A. It was asking Ricardo whether they have evaluated Cohane as
[14] a potential evaluator for the IOs and what kind of decision had
[15] they reached on that.
[16] Q. Mr. Mendez, if Doral already had an internal valuation and
[17] the Morgan Stanley valuation, what value would another external
[18] valuation be?
[19] A. It will provide further information about the evaluation of
[20] the instruments which were a significant estimate.
[21] Q. Are two external valuations better than one?
[22] A. Yes.
[23] Q. Mr. Mendez, what happened after you sent this e-mail?
[24] A. I remember that I coordinated or Ricardo coordinated a
[25] meeting, and we had a meeting with management to talk about the

[1] Stanley was obtaining valuations from a trading desk in the
[2] U.S.
[3] Q. Did you learn anything about whether or not Morgan
[4] Stanley's valuation was considering a floating nature of the
[5] IOs?
[6] A. He indicated that they were, they were aware, but it would
[7] not impact the valuation of the IOs.
[8] Q. I think you said he indicated. Can you tell us who
[9] indicated?
[10] A. Sammy Levis indicated to us in the meeting that Morgan
[11] Stanley, Jose Lopez from Morgan Stanley had told him that.
[12] Q. Mr. Mendez, was this meeting, was this documented by PWC in
[13] the work papers?
[14] A. Yes.
[15] Q. Could I ask you to turn to Government Exhibit 332. Mr.
[16] Mendez, do you recognize this document?
[17] A. Yes.
[18] Q. How do you recognize this document, Mr. Mendez?
[19] A. It is a working paper of the audit for the year ended
[20] December 31, '02.
[21] MR. ANTHONY: The government moves for the admission
[22] of Government Exhibit 332.
[23] THE COURT: Received.
[24] (Government Exhibit 332 received in evidence)
[25] BY MR. ANTHONY:

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[1] e-mail in further detail.
[2] Q. Drawing your attention to the e-mail at the top of the
[3] page, 7-30-2002, 7:22 pm, can you read the section beginning
[4] memo.
[5] A. "Memo. Don David feels comfortable with the requests but
[6] they want to meet with us to continue refining the process. I
[7] told them that you will be out until Wednesday, but they want
[8] to meet with me tomorrow afternoon to start talking about the
[9] process. I will attend the meeting with Arturo."
[10] Q. Was this the meeting that you were just referring to?
[11] A. Yes.
[12] Q. What do you remember happening at that meeting?
[13] A. I remember it was a meeting that took place in Ricardo
[14] Melendez's office at Doral. Arturo told one of the key
[15] members, and myself attended and Don David Levis and Ricardo
[16] Melendez participated, and I remember Sammy Levis participated
[17] at least a portion of the meeting.
[18] Q. The items you mentioned in the e-mail you just looked at,
[19] were those discussed?
[20] A. Yes.
[21] Q. Did you learn anything about what Morgan Stanley was doing
[22] at this meeting, the type of work it was to be performing?
[23] A. Yes, I recall that during the portion of the meeting that
[24] Sammy Levis participated, he indicated that based on his
[25] conversations with Morgan Stanley, he learned that Morgan

[1] Q. Mr. Mendez, I would like to turn your attention to the
[2] third page of this document. Can you identify the date for us
[3] on this document.
[4] A. July 31st, 2002.
[5] Q. And the subject?
[6] A. "Minutes-meeting with top management."
[7] Q. Who were the participants, according to this memo?
[8] A. It is described David Levis, Ricardo Melendez, Mario Levis,
[9] myself and Arturo Tous.
[10] Q. Would you read the first bullet point for us, please.
[11] A. "To be obtained from two independent brokers on a quarterly
[12] basis, one month prior to quarter-end. PWC will send the
[13] requests of quotation for the third quarter independently from
[14] the client and will receive direct replies from the brokers."
[15] Q. Can you explain what this bullet point is in reference to.
[16] A. It has two elements to it. The first sentence refers that
[17] management was going to obtain valuations from the two sources
[18] on a quarterly basis. The second sentence refers to the
[19] confirmation that it received was going to send to the
[20] evaluators.
[21] Q. Can you read the third bullet point for us in its entirety.
[22] A. "Prior to the meeting, Mario Levis discussed with Jose
[23] Lopez, Morgan Stanley, the process presently used by MS to
[24] obtain the quotations. On discussion with Mr. Levis, PWC
[25] learned that the quotes are obtained from Morgan Stanley's

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(1) loans and loan derivative instruments trading desk in the U.S.
(2) "Mario represented that Mr. Lopez indicated that the
(3) portfolio characteristics that determine the valuation factors
(4) are the WAC and the WAM. Mr. Levis stated that the valuation
(5) is not affected by the variable factor of the IOs and that
(6) according to his experience in the market and his discussions
(7) with Mr. Lopez, should not be."
(8) Q. Mr. Mendez, following this meeting did Doral, indeed,
(9) obtain a second external valuation of the interest-only strips?
(10) A. Yes.
(11) Q. Who did it obtain that valuation from?
(12) A. Popular Securities.
(13) Q. I think we have seen a couple of references to an external
(14) confirmation process. Is that right?
(15) A. Yes.
(16) Q. Did PWC engage that external confirmation process during
(17) this year?
(18) A. Yes.
(19) Q. Turn your attention to Government Exhibit 313. Mr. Mendez,
(20) do you recognize this document?
(21) A. Yes.
(22) Q. How do you recognize this document?
(23) A. It is a cover page of our working papers.
(24) Q. Do you recognize the documents behind it?
(25) A. Yes.

(1) what that process is.
(2) A. Management of the company will provide us a signed letter
(3) addressed to the party providing the confirmation. That letter
(4) will be provided to us, and we will mail, send a confirmation
(5) to the external party, and in a confirmation letter he will ask
(6) the external evaluator to provide a copy directly to the
(7) auditors.
(8) (Continued on next page)
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(1) Q. Are these documents from your work papers as well?
(2) A. Yes.
(3) MR. ANTHONY: Your Honor, the government moves for the
(4) admission of Government Exhibit 313.
(5) THE COURT: Received.
(6) (Government Exhibit 313 received in evidence)
(7) BY MR. ANTHONY:
(8) Q. Mr. Mendez, could you turn to the fourth page of this
(9) document. Can you explain to us what this page is, what this
(10) document is.
(11) A. This page refers to the audit confirmation I mentioned
(12) earlier signed by management and addressed to the external
(13) evaluator Popular Securities in this case.
(14) Q. Why was Mario Samuel Levis sending this letter?
(15) A. He was at that time the treasurer of the company and the
(16) contact for the IOs.
(17) Q. Did you also understand he was the contact with the
(18) external valuation parties?
(19) A. Yeah, that was my understanding.
(20) Q. Would you turn to the next page, please. What is this
(21) document?
(22) A. The audit confirmation request to Jose Lopez from Morgan
(23) Stanley.
(24) Q. I think you described for us earlier a process by which
(25) these confirmations were sent. Could you briefly remind us

(1) BY MR. ANTHONY:
(2) Q. Mr. Mendez, may I ask you to turn to the second and third
(3) pages of this document and ask you to identify what those pages
(4) are.
(5) A. This was a letter containing the valuation provided by
(6) Popular Securities.
(7) Q. Let me also ask you to turn to the 12th page of this
(8) document. Mr. Mendez, this 12th page, through the end of the
(9) document, can you identify what these pages are?
(10) A. The response from Morgan Stanley to the valuation request.
(11) Q. Is this similar to the Morgan Stanley valuation we looked
(12) at earlier?
(13) A. Yes.
(14) Q. Does it work in the same way?
(15) A. Yes.
(16) Q. By the end of calendar year 2002, had anyone on the PWC
(17) audit team in Puerto Rico been able to speak with Morgan
(18) Stanley or anyone at Banco Popular?
(19) A. Could you repeat the question again, please?
(20) Q. Sure. By the end of the calendar year 2002, had anyone on
(21) your audit team in Puerto Rico working on the Doral audit, had
(22) anyone spoken with Morgan Stanley or Popular Securities
(23) regarding the valuation work they were doing for Doral?
(24) A. No.
(25) Q. Did you make any additional attempts in connection with the

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[1] year end 2002 audit to do so?

[2] **A.** Yes.

[3] **Q.** What did you do?

[4] **A.** I remember the meetings or conversations with Morgan

[5] Stanley, Popular Securities, with management, and at some point

[6] in early 2003, before the completion of the audit we had the

[7] opportunity of meeting or talking to the valuers.

[8] **Q.** May I ask you to turn to Government Exhibit 307.

[9] Mr. Mendez, do you recognize this document?

[10] **A.** Yes.

[11] **Q.** How do you recognize this document?

[12] **A.** It's an e-mail where I'm, I participate or I received, and

[13] I remember it from my time in the audit period.

[14] **MR. ANTHONY:** Your Honor, the government moves for the

[15] admission of Government Exhibit 307.

[16] **THE COURT:** Received.

[17] (Government's Exhibit 307 received in evidence)

[18] **BY MR. ANTHONY:**

[19] **Q.** Mr. Mendez, while I realize you didn't send it, could you

[20] read the first e-mail in this chain, the one on Tuesday,

[21] February 17, at 2:35 for us, please?

[22] **A.** "Carlos Mendez from PWC is requesting telephone meetings

[23] with Joe Lopez and Juany Ortiz to understand and document in

[24] their work papers the underlying assumptions used by them to

[25] arrive at values shown in November valuations."

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[1] **Q.** Why were you requesting such meetings with Joe Lopez and

[2] Juan Ortiz?

[3] **A.** To have the opportunity of obtaining further understanding

[4] as to the sources of their valuations.

[5] **Q.** Mr. Mendez, could you read the response from Sammy Levis in

[6] February 19, 2003, at 10:30 a.m.?

[7] **A.** "Tell him that Joe Lopez doesn't use assumptions. It is a

[8] market quote. Juany's valuation is an investment banking

[9] valuation which uses assumptions. If he wants to, he can talk

[10] to Juany, 766-4164. He should not speak to Joe because all

[11] that Joe does is to call his trader in New York City and get a

[12] quote. We have explained this to him in the past."

[13] **Q.** Had Mr. Levis explained this to you in the past?

[14] **A.** Yes.

[15] **Q.** And when was that?

[16] **A.** In the meeting that was in the summer, in the summer of

[17] 2002.

[18] **Q.** Is that the one that was just recorded in the memo we just

[19] looked at?

[20] **A.** Yes.

[21] **Q.** Mr. Mendez, could I ask you now to turn to Government

[22] Exhibit 308.

[23] Mr. Mendez, do you recognize this document?

[24] **A.** Yes.

[25] **Q.** How do you recognize this document?

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[1] **A.** It's a chain of e-mails where, that I received, and I

[2] remember it from my period in the engagement.

[3] **MR. ANTHONY:** Your Honor, the government moves the

[4] admission of Government Exhibit 308.

[5] **THE COURT:** Received.

[6] (Government's Exhibit 308 received in evidence)

[7] **BY MR. ANTHONY:**

[8] **Q.** Mr. Mendez, I know it's a bit of a long e-mail, but would

[9] you mind reading for us your e-mail on February 19, 2003, at

[10] 4:08 p.m.?

[11] **A.** "Ricardo, as discussed with you, I'm fully aware of Don

[12] David and Sammy's explanation about the source of pricing used

[13] by Joe Lopez. However, my concern is not the source of the

[14] pricing, but if the source is considering all the

[15] characteristics of the instruments. Furthermore, the GAAP

[16] definition of fair value is the following:

[17] "The amount at which that asset (or liability) could be

[18] bought (or incurred) or sold (or settled) in a current

[19] transactions between willing parties, that is, other than in

[20] forced or liquidation sale.

[21] "Based on this, the provisional standards require PWC to

[22] ascertain that the market quotations received from Morgan

[23] Stanley represent indeed the fair value of Doral's IOs

[24] considering all their characteristics. These standards also

[25] require us to corroborate management's explanation.

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[1] "I believe that Joe Lopez and/or Morgan Stanley's trading

[2] desk can answer our question in a few minutes and will permit

[3] us to comply with the professional standards. I will call you

[4] to discuss. Regards Carlos."

[5] **Q.** Why do you quote the GAAP language in this e-mail?

[6] **A.** To make it clear as to what was the fair value definition

[7] and what we wanted to confirm with Morgan Stanley.

[8] **Q.** Can you read the response at the top of the page?

[9] **A.** "Ricardo, make sure that PWC understands that we do not

[10] oppose them talking to Joe Lopez nor Juany Ortiz. I just want

[11] to make sure that this action is really required since they

[12] have already talked to them in the past. Also, these people

[13] are busy, and I don't want to bother them unless it is

[14] absolutely necessary. If they really need to talk to Joe or

[15] Juany, they have my okay to call them. I would appreciate it

[16] if I can be in the call just to make sure that there are no

[17] misunderstandings; sometimes the brokers use different

[18] terminology. If they don't want me in the call, that's fine

[19] too. Let me know when and if I can be in the call. Regards,

[20] Sammy."

[21] **Q.** Did you have any objection to Sammy Levis participating in

[22] the call?

[23] **A.** No.

[24] **Q.** Did you indeed speak with people at Morgan Stanley and

[25] Popular Securities in connection with your work on the 2002

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[1] Doral?
[2] A. Yes.
[3] Q. Let's start with Morgan Stanley. What can you tell us
[4] about that conversation?
[5] A. I remember it was a telephone conversation that I took a
[6] call when I was in my PWC office, and I received a call from
[7] Ricardo Melendez and Jose Lopez from Morgan Stanley, and I
[8] believe but don't recall if Sammy Levis was on the call.
[9] Q. What did you learn during this call about the type of work
[10] that Morgan Stanley was performing?
[11] A. That they were obtaining the valuation for the IOs from the
[12] trading desk in the U.S.
[13] Q. Did you repeat the GAAP language that we just looked at
[14] from your e-mail?
[15] A. Yes, I described the language to Mr. Lopez.
[16] Q. What was your purpose for doing that?
[17] A. Confirm that he had an understanding of the GAAP
[18] definition, which was the purpose of the valuation.
[19] Q. Did you discuss the fixed rate feature of some Doral IOs at
[20] all?
[21] A. I inquired Mr. Lopez if he had an understanding of the
[22] feature, and whether they had, Morgan Stanley had all the
[23] information that they needed to provide a GAAP valuation for
[24] the IOs.
[25] Q. And what did Mr. Lopez say in response?

[1] Q. Could I now turn your attention to Government Exhibits 325?
[2] Mr. Mendez, do you recognize this document?
[3] A. Yes.
[4] Q. How do you recognize this document?
[5] A. It is a working paper for the audit of the financial
[6] statement for 2002.
[7] MR. ANTHONY: Your Honor, the government moves for the
[8] admission of Government Exhibit 325.
[9] THE COURT: Received.
[10] (Government's Exhibit 325 received in evidence)
[11] BY MR. ANTHONY:
[12] Q. Mr. Mendez, I'd like to turn your attention to the second
[13] page of this document, to the second just below the icon in the
[14] middle of the page. Could you read the sentence on top of that
[15] session beginning "throughout the year"?
[16] A. Can you repeat, indicate where the sentence again?
[17] Q. Just below the icon, the sentence beginning "throughout the
[18] year."
[19] A. Okay. "Throughout the year and driven by both, PWC's
[20] recommendations and management initiative, the company
[21] continued enhancing its procedures as follows."
[22] Q. Can you describe how the company enhanced its valuation
[23] procedures as part of the 2002 audit year?
[24] A. They obtained a fair value valuation from Popular
[25] Securities.

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[1] A. Yes. He affirmed that.
[2] Q. Did you also have a conversation with Popular Securities?
[3] A. Yes.
[4] Q. Can you tell us about that conversation?
[5] A. For Popular Securities, we had a meeting, at Popular
[6] Securities. That meeting, Ramon Ponte, Arturo Tous, there were
[7] a number of participants, and from PWC, Ramon Ponte, Arturo
[8] Tous, and myself went to the meeting. From Doral, Ricardo
[9] Melendez participated. And I believe that based on my
[10] recollection, Luis Aponte participate. From Popular
[11] Securities, Carlos Ortiz and a number of his staff
[12] participated.
[13] Q. And during that meeting, did you learn what type of
[14] valuation that Popular Securities was performing?
[15] A. Yes.
[16] Q. What type were they performing?
[17] A. They were doing a discounted cash flow valuation.
[18] Q. Who was determining the inputs to that language, at least
[19] as you understood it?
[20] A. Could you repeat the question again.
[21] Q. Sure. I'll move on.
[22] Mr. Mendez, did you document the conversations you had
[23] with Joe Lopez at Morgan Stanley and Popular Securities in the
[24] work papers?
[25] A. Yes.

[1] Q. Mr. Mendez, just below that bullet point, it reads, "Note
[2] that we met Carlos Ortiz and his assistants from PS and Ricardo
[3] Melendez, and we discussed the following matters."
[4] What is the sentence below that referring to?
[5] A. It summarizes information that we learned during the
[6] meeting with Popular Securities.
[7] Q. Let's talk about how or the types of inputs that go into
[8] the Popular Securities model.
[9] A. Yes.
[10] Q. What are some of those inputs.
[11] A. Prepayment speeds, discount rates, and those were some of
[12] the basic assumptions.
[13] Q. Was it your understanding that Popular Securities was
[14] independently determining those inputs, those assumptions?
[15] A. Yes.
[16] Q. If you could turn to the next page, do you see the second
[17] point in the top of the page labeled the "floating IOs versus
[18] fixed IOs"?
[19] A. Yes.
[20] Q. Could you read that section for us?
[21] A. "He explained that they have not included the floating
[22] aspect of the IOs in the valuation because he considers that it
[23] will add another variable to the model which is offset in some
[24] way by the impact in the prepayment speed of the portfolios.
[25] Furthermore, his views are that in periods of interest rate

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[1] curves that are fairly flat (i.e., 2002), the effect may be
 [2] considered minor and the static analysis is considered more
 [3] accurate. Nonetheless, he said that the impact of such
 [4] variable should be considered in other scenarios where the
 [5] spread obtained could be impacted by higher LIBOR."
 [6] **Q.** Is it your understanding that if Popular Securities did
 [7] decide that higher LIBOR could impact the valuations they would
 [8] take that particular fact into account?
 [9] **A.** That was my understanding.
 [10] **Q.** Mr. Mendez, at this point, what was the process that the
 [11] company was using to determine the fair value of its IOs in its
 [12] financial statements?
 [13] **A.** The company was obtaining valuations from Morgan Stanley
 [14] and Popular Securities and having an internal valuation on
 [15] their discounted cash flow models.
 [16] **Q.** This paper also refers at the beginning of the middle of
 [17] the third page to assessment of fair value and underlying
 [18] assumptions section. Do you see that?
 [19] **A.** Sorry. What page are you referring to?
 [20] **Q.** On the third page, just under the icon, the IO schedule
 [21] icon.
 [22] **A.** Okay. I see it.
 [23] **Q.** In that first bullet point, it says, "Management and
 [24] Popular Securities both indicated that the variable spread
 [25] factor is typically not considered in determining fair value

[1] 2002.
 [2] **Q.** Is this audit report or audit opinion similar to the one we
 [3] looked at in connection with the 2001 audit?
 [4] **A.** Yes.
 [5] **Q.** I ask you to turn the page and find for us the place on the
 [6] balance sheet where the IOs are contained.
 [7] **THE COURT:** Are you offering this?
 [8] **MR. ANTHONY:** Your Honor, I believe this is already in
 [9] evidence.
 [10] **THE COURT:** It is, okay. That's right. For 2002.
 [11] **MR. ANTHONY:** 2002 10K.
 [12] **THE COURT:** Okay.
 [13] **A.** Under the caption "other investment securities, trading
 [14] securities at fair value."
 [15] **Q.** Could you read for us the value in 2001 and 2002?
 [16] **A.** For 2002, the balance was 412,846,000, and for 2001,
 [17] 236,829,000.
 [18] **Q.** Could I ask you to turn the page and find the location
 [19] where Doral's noncash gain-on-sale income -- let's just refer
 [20] to where its gain-on-sale income for the IOs is contained.
 [21] **A.** It was included under the caption noninterest income net
 [22] gain on mortgage loan sales increase.
 [23] **Q.** Could you read for us the values for 2000, 2001 and 2002?
 [24] **A.** For 2002, 220,585,000. For 2001, 187,221,000. For 2000,
 [25] it was 134,339,000.

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[1] and that the impact, if any, would not be significant,
 [2] considering the subjective nature of the estimates involved.
 [3] Further, static analysis is the prevailing model used in market
 [4] transactions."
 [5] Did PWC do anything to test those representations?
 [6] **A.** We inquired them about their basis for those
 [7] representations and we performed some high-level analysis to
 [8] valuate potential impacts of IO rates in the valuation that
 [9] management was providing, and we performed some analysis.
 [10] **Q.** In connection with the 2002 audit, the analysis that you
 [11] performed, the internal model, the Popular Securities model,
 [12] and the Morgan Stanley model, which of those carried the most
 [13] weight insofar as the audit team was concerned when assessing
 [14] the value of Doral's IOs?
 [15] **A.** The external valuations carried significant weight, both
 [16] valuations from the additional parties.
 [17] **Q.** Mr. Mendez, can I ask you to turn to the next exhibit in
 [18] your binder, GX6202, and I believe this is an excerpt from a
 [19] document that is already in evidence.
 [20] Mr. Mendez, do you recognize this document?
 [21] **A.** Yes.
 [22] **Q.** Can I get you to turn to the fourth page? Sorry. It's the
 [23] fifth page. What is contained here on the fifth page of this
 [24] document?
 [25] **A.** It is the audit report for the year ended December 31,

[1] **Q.** Mr. Mendez, could I ask you to turn to the 13th page of
 [2] this document, note 2, summary of significant accounting
 [3] policies. Can you remind us what a significant accounting
 [4] policy is?
 [5] **THE COURT:** What was the question?
 [6] **MR. ANTHONY:** If Mr. Mendez could remind us what a
 [7] significant accounting policy is.
 [8] **A.** It is a description of the significant accounting policies
 [9] followed by the company in preparing its financial statements.
 [10] **Q.** Could you turn the page and read for us the section
 [11] beginning with "in connection," that carries over to the next
 [12] page.
 [13] **A.** "In connection with the securitization transactions and the
 [14] sale of loans, the company recognizes as interest-only strips
 [15] (IOs) the rights to cash flows remaining after the payment of
 [16] the servicing fees and the contractual payments to the buyers
 [17] of the loans. The contractual payments to the buyers are
 [18] generally based on a spread over LIBOR. The contractual
 [19] payments are either fixed over the life of the loans or
 [20] floating with quarterly resetting. These IOs are carried at
 [21] fair value, which is generally determined based on dealers'
 [22] quotes or market prices for sales of similar assets. The
 [23] company also evaluates the fair value of IOs using external and
 [24] internal valuations based on discounted cash flow models that
 [25] incorporate assumptions regarding discount rates and mortgage

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(1) prepayment rates."
(2) Q. Mr. Mendez, the dealer quotes referenced in this section,
(3) did you have an understanding of what that referred to?
(4) A. The Morgan Stanley valuation.
(5) Q. And how about the external valuation based on discounted
(6) cash flow models?
(7) A. Sorry. Could you repeat the question again?
(8) Q. Yes. How about the external valuation based on discounted
(9) cash flow models?
(10) A. That was the one provided by Popular Securities.
(11) Q. Mr. Mendez, when you were at PWC, and the audit team was
(12) assessing the value of Doral's interest-only strips, did the
(13) audit team take the value of any hedges Doral had into account
(14) when assessing the value of the interest-only strips?
(15) A. No.
(16) Q. Why not?
(17) A. Because those were separate contracts.
(18) Q. They're separate from the IOs?
(19) A. Yes.
(20) MR. ANTHONY: Your Honor, if I may have just one
(21) second to confer with my colleagues.
(22) Q. Mr. Mendez, just one or two more questions for you. May I
(23) turn your attention to page 28 of this excerpt, note 5,
(24) securities held for trading. We're still in Government Exhibit
(25) 6202.

(1) THE WITNESS: Based on market multiples or market
(2) valuations. Based on information that they had from their
(3) trading desk.
(4) THE COURT: So the trading desk would give them some
(5) information that would lead them to this market multiple,
(6) right?
(7) THE WITNESS: Yes.
(8) THE COURT: And the market multiple was to take the
(9) total face value of the mortgages, right?
(10) THE WITNESS: Yes.
(11) THE COURT: And then multiply that by a percentage,
(12) right?
(13) THE WITNESS: Yes.
(14) THE COURT: And the percentage or average percentage
(15) that they were getting on the interest-only strips, right?
(16) Their portion. Let me say it again.
(17) For each pool, there was a percentage that they were
(18) getting on their interest-only strip, right?
(19) THE WITNESS: Yes.
(20) THE COURT: And those interest-only strip amounts were
(21) average for all the pools, right? Am I right or wrong?
(22) THE WITNESS: Yes. They were getting different
(23) interest rates from the different transactions that they made.
(24) THE COURT: And to get the figure they used in this
(25) calculation of value, were they average, or not?

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(1) A. Yes.
(2) Q. Describe for us what is here in note 5.
(3) A. A description of the securities owned by the company
(4) classified as trading securities.
(5) Q. And can you read the value for the interest-only strips
(6) contained in this note 5?
(7) A. At December 31, 2002, it was 359,185,000. At December 31,
(8) 2001, it was 236,468,000.
(9) MR. ANTHONY: Your Honor, at this time, the government
(10) has no further questions.
(11) THE COURT: I just want to make sure that I
(12) understand. As of the end of your work on the 2002 audit, it
(13) was your understanding that Doral had two independent
(14) evaluators, right?
(15) THE WITNESS: Yes.
(16) THE COURT: And then Doral made its own evaluation,
(17) right?
(18) THE WITNESS: Yes.
(19) THE COURT: And maybe I didn't get this, but, for the
(20) independent evaluators, were there two different methods that
(21) they were using, according to your understanding?
(22) THE WITNESS: Yes, that's correct.
(23) THE COURT: I think you described it, and it's
(24) probably in the documents, but do you mind describing it again?
(25) What method was Morgan Stanley using?

(1) THE WITNESS: My understanding was providing multiples
(2) by different set of pools, so, I'm trying to follow your
(3) comment.
(4) THE COURT: How did it work? In other words, was
(5) there a calculation for each pool?
(6) THE WITNESS: Yes, for a group of pools, Morgan
(7) Stanley would provide a multiple that multiplying that --
(8) THE COURT: Before we get to the multiple --
(9) THE WITNESS: Yes.
(10) THE COURT: -- we've got to get the percentage for the
(11) interest-only strip.
(12) THE WITNESS: Right.
(13) THE COURT: Don't we?
(14) THE WITNESS: Yes.
(15) THE COURT: And that percentage is multiplied by the
(16) whole value of the mortgages, right?
(17) THE WITNESS: Yes.
(18) THE COURT: All right. So in some way, and I won't
(19) get into this, they had a percentage figure for the
(20) interest-only strips?
(21) THE WITNESS: Yes.
(22) THE COURT: And that was multiplied by all the
(23) mortgages?
(24) THE WITNESS: Yes.
(25) THE COURT: And so that would result in some figure,

Exhibit K

In The Matter Of:

*UNITED STATES OF AMERICA v.
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*VOLUME 16
April 19, 2010*

*TRIAL
SOUTHERN DISTRICT REPORTERS
500 PEARL STREET
NEW YORK, NY 10007
212-805-0300*

Original File 04JWLEVF.txt, Pages 2375-2580 (206)

Word Index included with this Min-U-Script®

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[1] I said I don't think you should be a broker because,
[2] my son, since he was raised in Puerto Rico, he wasn't that
[3] fluent in English, and I thought he would have a hard time.

[4] Give me a chance and let me see if I could help you
[5] get a job. I checked around a couple of places. I checked
[6] with Sammy. Sammy gave me one of his subordinates to call. I
[7] gave my son the information. My son called that person. He
[8] was interviewed and hired as a clerk, worked in Doral for 2005
[9] making about low 20,000 a year. He didn't have a big position,
[10] just a clerk there.

[11] Q. When did your son leave Doral?

[12] A. He left Doral in 2006.

[13] Q. When did you first meet the defendant, Sammy Levis?

[14] You said your relationship with the family began back
[15] in 1982 with David Levis. When did you first meet Sammy Levis?

[16] A. I met Sammy Levis when Sammy Levis joined Doral Financial,
[17] for Sammy Levis used to work for Merrill Lynch back in the late
[18] 80's, early 90's.

[19] When there was a downsizing in Merrill Lynch, Sammy
[20] more or less was out of a job and he was hired by Doral. That
[21] is when I met Sammy.

[22] Q. Prior to 2001, the only business you were doing with Doral
[23] were these transactions where you were loaning them money in
[24] exchange for collateral they were putting up?

[25] A. Yes, sir.

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[1] Q. Did you socialize with the defendant at all?

[2] A. My wife and I are not too socially-going people. We go to
[3] a lot of activities, but the Levis family had a fundraiser that
[4] we would do once a year to help children with cancer. My wife
[5] and I always went to that activity.

[6] The only other activity I remember socializing with
[7] Sammy was when he got married, he invited me to the wedding and
[8] I went with my wife. When we got to the hall, everybody from
[9] the street was there, all his friends, bankers and brokers and
[10] everything. Basically those are the only times I really
[11] socialized with Sammy.

[12] Q. How would you describe your professional relationship with
[13] the defendant?

[14] A. Well, Sammy and I had a very good relationship over the
[15] years. We talked a lot about the market and we tried to do
[16] business, sometimes we couldn't because they were a very
[17] competitive firm. We had two components with other brokers. I
[18] considered it a very good relationship and at the time I
[19] considered Sammy a good friend.

[20] Q. Approximately when did the issue of you performing a
[21] valuation of Doral's IOs first come up?

[22] A. They came up in 2001.

[23] Q. Can you tell us how it came up, who contacted you?

[24] A. I got a call from Sammy one day, I don't remember morning
[25] or afternoon. He called me and said I need to you to help me

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[1] with something. What I can help you? I will send you
[2] something by messenger. When you get it, call me and we'll
[3] discuss it. He sent me an envelope and he sent me a listing,
[4] and I called him, and it was a listing of IOs.

[5] Sammy started describing this type of instrument, the
[6] first time I heard about it when he showed it to me.

[7] Q. How familiar were you with IOs?

[8] A. I never dealt with IOs before then. Basically IO is Doral
[9] used to sell their nonconforming mortgages to financial
[10] institutions in Puerto Rico because in Puerto Rico there is a
[11] scarcity of Puerto Rico assets and the banks have these ratios
[12] they have to maintain. In Puerto Rico they have to have so
[13] many Puerto Rico assets against U.S. assets.

[14] The banks would go to mortgage bankers like Sammy, and
[15] they would buy nonconforming mortgages, and Sammy would sell
[16] them at a floating rate. I was never involved in the setting
[17] up what, what price he would sell it to them. Basically Doral
[18] had a transaction where they were getting a fixed rate. For
[19] example, 8 percent fixed coupon and they would sell it to a
[20] bank at a floating rate on monthly basis, maybe the bank was
[21] getting 5 percent, so Doral was really getting a 3 point spread.
[22] carry, meaning they would getting 8 percent on the mortgages at
[23] issue and paying the banks 15.

[24] So that 3 points is like a cash flow because you get
[25] more cash in than what you're paying out. So you have to price

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[1] that cash flow because it is really a part of a security that
[2] is generating an income. He started explaining to me that
[3] these mortgages have a weighted average coupon, weighted
[4] average maturity, and that they act familiar to regular
[5] mortgages in Puerto Rico, and you have to get a similar
[6] security that has the same characteristics, meaning 8 percent
[7] coupon, 2 -- as an example, 233 months, divide by 12 and gives
[8] you X amount of years, say 15 years and go into the market and
[9] theoretically find matching or close to matching security with
[10] those characteristics.

[11] And what you would do is you would go into a simple
[12] example, you call into Bloomberg, you find a similar security
[13] and that system will analyze it for you and tell you how those
[14] mortgages with those characteristics are repaying. Mortgages
[15] prepay on monthly basis because people make principal payment
[16] every month and that affects the group of of mortgages. Every
[17] month they keep paying down.

[18] Q. This is all -- sorry, Mr. Lopez -- this is all information
[19] that the defendant is explaining to you?

[20] A. Yes, yes. For a minute I thought Sammy, I don't know how
[21] to do this. This is Chinese to me. I really don't know. We
[22] talked. He said I don't need your help to do this. Somebody
[23] will do this for you. He said I can't. He told me one or two
[24] other people.

[25] Since the relationship I had with him, I considered

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[11] him a friend, respected the family, an executive vice president
[12] and treasurer, I figured he said this will be used for my
[13] internal use only, and he convinced me and I signed off. What
[14] Sammy Levis was giving me was the numbers that he used, and I
[15] would sign off I was doing the numbers.

[16] Since those mortgages were generated from Doral and
[17] Doral had all the information on those mortgages, the way
[18] they're prepaid, if anybody knew what those mortgages were
[19] prepaying and what they were more or less worth, it would be
[20] Sammy. So I trusted him and signed off. This went on for a
[21] couple of years, from 2004 he would send me -- not every
[22] quarter, send me every couple of months send me a short listing
[23] and I would initial I had done it. I would take the
[24] information he gave it to me and send it back by messenger.

[15] Q. Let's step back. In that conversation with the defendant,
[16] you asked him whether he had anybody else pricing these
[17] instruments, these interest-only strips?

[18] A. Yes, he did. He told me he had one or two other people
[19] doing it on the street, but he didn't tell me who.

[20] Q. Did he tell you why?

[21] A. Because it was confidential.

[22] THE COURT: Look, you need to try to speak slower.

[23] THE WITNESS: Okay.

[24] THE COURT: You are very, very fast. It is hard to
[25] get it.

[11] A. No.

[12] Q. Mr. Lopez, why did you agree to do something, sign off on
[13] something you're not actually doing?

[14] A. You know, in Puerto Rico, the Puerto Rico market is a small,
[15] market. Everybody knows each other and after a while clients
[16] are more friends than clients, and it is a closely-held
[17] community. After a while you respect people, and I figured
[18] that he wasn't doing anything wrong, I decided to do it. I
[19] trusted him.

[10] Q. How long was this conversation?

[11] A. Very brief, maybe 10, 15 minutes.

[12] Q. So after this conversation where you agreed to sign off on
[13] the numbers, what happens next? You said you received
[14] packages?

[15] THE COURT: Received what?

[16] THE WITNESS: When I agreed to do the numbers for
[17] Doral, he was sending me a package, an envelope with the
[18] documents I would have to initial and sign and I would send it
[19] back to him.

[20] BY MR. STELLMACH:

[21] Q. How were those packages delivered to you?

[22] A. By one of his messengers.

[23] Q. Explain to us what was inside the packages you received
[24] from the defendant.

[25] A. He would send me a listing with all the numbers already

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[11] THE WITNESS: Sorry, your Honor.

[12] BY MR. STELLMACH:

[13] Q. And when the defendant told you that the numbers that he
[14] wanted from you would be used for his internal purposes, what
[15] did you understand that to mean?

[16] A. He was going to use it for his probably his own personal
[17] use. I was never told they were going to be used for anything
[18] other than that.

[19] Q. I think you said that this was all new to you and you
[20] didn't really understand it?

[11] A. Yes, sir.

[12] Q. Did you tell that to Mr. Levis?

[13] A. He knew it. I said Sammy, like I said before, this is
[14] Chinese to me. I don't trade these instruments. I don't know
[15] how to price these. He said Joe, trust me, you are not doing
[16] anything wrong. I decided to help him.

[17] Q. Did you tell Mr. Levis you would try to do this valuation
[18] yourself?

[19] A. No.

[20] Q. Did he ever ask you whether anyone else at Morgan Stanley
[21] that you knew could possibly do this type of evaluation?

[22] A. No.

[23] Q. Or whether you could recommend somebody else either at
[24] Morgan Stanley or another firm that could actually do the
[25] valuation?

[11] done and he would send me another listing that didn't have the
[12] numbers. What I would do is transpose numbers from listing to
[13] another, initial and signed it and send it back.

[14] Q. When you said listing --

[15] A. A spreadsheet that had the IOs information, the coupon,
[16] maturity, the amount.

[17] Q. So one spreadsheet, these spreadsheets were identical?

[18] A. Yes, they were identical.

[19] Q. Except one spreadsheet already had valuations written on
[20] it?

[11] A. Yes, sir.

[12] Q. You would transpose the numbers. Could you just explain
[13] what you mean by that.

[14] A. He would send me a listing that was completely filled out
[15] that had the valuation, the multiple, which is a number you
[16] arrive at after you look at the prepayment speeds and make
[17] adjustments because in Puerto Rico mortgages, he would send me
[18] two identical sheets, set of sheets. One of them had the
[19] numbers and one was in blank. I transposed the numbers to the
[20] one that was in blank and filled out the blanks and just send
[21] it back to him.

[22] Q. When you spoke with the defendant, did he make clear to you
[23] that all you were supposed to do was just recopy the numbers?

[24] A. Yes, sir.

[25] Q. So what independent work did you do on this project?

Exhibit L

In The Matter Of:

*UNITED STATES OF AMERICA v.
MARIO S. LEVIS A/K/A SAMMY LEVIS*

*VOLUME 11
April 12, 2010*

*TRIAL
SOUTHERN DISTRICT REPORTERS
500 PEARL STREET
NEW YORK, NY 10007
212-805-0300*

Original File 04CWLEVF.txt, Pages 1621-1755 (135)

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April 12, 2010

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(1) years and moved on to investment banking at a firm called at
(2) that time Paine Webber, which is now part of UBS.

(3) After a few years at UBS, I left to go into government, in
(4) the Puerto Rico, called the Government Development Bank for
(5) Puerto Rico, which is their central bank. I was executive vice
(6) president in charge of public and private financing, executive
(7) director of the Puerto Rico industrial, medical, and pollution
(8) control facilities financing authority and Caribbean financing
(9) authorities as well.

(10) After approximately 3.3 years in government, I went, became
(11) a consultant in the waste energy field, with the San Juan Waste
(12) Management Authority in Puerto Rico, ran a micro-fund for them,
(13) and then after that, I went to Prudential Securities in Puerto
(14) Rico and went to offices in New York, head of Latin American
(15) banking for them and head of international banking at
(16) Prudential Securities.

(17) After Prudential, that sold to Wachovia, which is now part
(18) of Wells Fargo, I decided to come back to Puerto Rico and
(19) joined Popular Securities in 2003.

(20) Q. Was that approximately September of 2003?

(21) A. First week of September 2003.

(22) Q. Can you explain to us what the relationship is between
(23) Popular Securities and Banco Popular?

(24) A. They're affiliates. Both are owned by Popular, Inc., which
(25) is the publicly traded company, Banco Popular and Popular

(1) to Doral?

(2) A. At the time I arrived in September of 2003, in the
(3) investment banking area specifically, we were undertaking a,
(4) what we call valuation of their IO mortgage portfolio at that
(5) time.

(6) Q. And prior to joining Popular, what experience did you have
(7) in valuing assets?

(8) A. As an investment banker, in previous firms that I
(9) mentioned, I had done valuations of companies in Mexico. I was
(10) in charge of the valuation of the sugar industry for the
(11) Mexican government, then purchase of a broker-dealer for
(12) Prudential internally being their mergers and acquisition
(13) banker in the transaction. So I was familiar with valuing
(14) assets and valuing companies.

(15) Q. Were you familiar with the concept of an independent
(16) valuation?

(17) A. I was and I am familiar with the concept of an independent
(18) valuation.

(19) Q. And could you explain for us what makes a valuation
(20) independent, from your perspective?

(21) A. I think it's, from my perspective, it's something that the
(22) word "independence" connotes. You don't -- you do it on,
(23) basically, your own, your own value judgments, your own
(24) criteria. You're supposed to be independent, arm's length from
(25) the company or the entity that you're working for. You're

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(1) Securities.

(2) Q. And in general terms, what were your responsibilities at
(3) Popular Securities?

(4) A. I was hired to be the head of the investment banking area.
(5) We had a group of at that time four other employees in
(6) investment banking and we were a division of Popular Securities
(7) that also included an institutional trading area as well as any
(8) retail brokerage area. That was the three parts of Popular
(9) Securities at that time.

(10) Q. And so just in general terms, what were your
(11) responsibilities on a day-to-day basis in the investment
(12) banking division at Popular Securities?

(13) A. I was obviously to make sure that the, as any manager, to
(14) run the operation, be responsible for, ultimately responsible
(15) for the decisions that the group made, the going after new
(16) business as well as executing on existing business that we had.
(17) Personnel issues, compliance issues, all the normal issues that
(18) a manager would have in running a business.

(19) Q. Are you familiar with a company called Doral Financial
(20) Corporation?

(21) A. Yes, I am.

(22) Q. At the time that you joined Popular Securities, was Doral a
(23) client of the firm?

(24) A. It was.

(25) Q. And what types of services was Popular Securities providing

(1) supposed to come up with a value, depending on what the nature
(2) of the transaction. If it's a valuation, you're supposed to do
(3) it independently. I think it's something that, you know, facts
(4) and circumstances, but I think intrinsically you're not swayed.
(5) You have your own independent judgment when you undertake that
(6) valuation, and the criteria you use are independent in material
(7) respects.

(8) Q. And we'll go through this in more detail later, but was the
(9) valuation that Popular was performing of Doral's IO portfolio
(10) independent?

(11) A. In my, in my mind, no, it was not.

(12) Q. Why not?

(13) A. Well, from the get-go, the -- if somebody is relying or
(14) there is a certain notion that it's supposed to be independent,
(15) I think the ultimate value that you're trying to ascertain has
(16) to come from the criteria that you've established as being
(17) something that you're comfortable with that you would arrive at
(18) on your own judgment and on your own work product, and I think
(19) from the start, just to give you an example, the mortgages that
(20) we were, the raw data that we were getting from Doral when I
(21) arrived there and I was explained the nature of the assignment,
(22) we weren't even checking those mortgages existed. We didn't do
(23) any diligence, which is a word you use when you go and check
(24) and make sure that the actual assets exist.

(25) In the case of valuing an oil company, you want to make

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[1] sure there's oil in the gas tanks. You go kick the tires of
[2] the business, to make sure it exists. Fundamentally we didn't
[3] even check that the mortgages were there. We took it at face
[4] value, so to me that's, No. 1, a kind of criteria I wanted to
[5] ascertain that they actually existed.

[6] I can keep going, if you like.

[7] **Q.** Just in general terms, were there other assumptions on
[8] which you just didn't kick tires, you accepted at face value
[9] representations from the company itself?

[10] **A.** The nature of those mortgages, the coupons. The
[11] maturities, the actual documents that supported them, that
[12] existed in itself was one major criteria. There were other
[13] criteria that were material to the valuation that we got from
[14] Doral.

[15] **Q.** We'll go through those in more detail later, could you just
[16] tell us what those other criteria were that you were getting
[17] from Doral?

[18] **A.** Well -- as I say, there was like a, there was a fundamental
[19] one, which was the nature and especially important in an IO
[20] portfolio, the existence of a cap that we were told, you know,
[21] by them directly that there was a rate that they had
[22] negotiated, purchased at that time, we can get into how they
[23] explained it to us, but that basically affected the cash flows
[24] that were the nature of the valuation that we were doing.
[25] That's one criteria.

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[1] There were certain loans that were paid off that we would
[2] add back to the pools that we would normally have not done if
[3] we were doing an independent valuation, or at least we would
[4] have explained to whoever was relying on our opinion as to what
[5] we were doing that I thought also was important in the
[6] valuation.

[7] **Q.** Who at Doral was your contact?

[8] **THE COURT:** It was a long answer. But could the
[9] reporter read that.

[10] (Record read)

[11] **BY MR. STELLMACH:**

[12] **Q.** Who at Doral was your contact in providing the criteria
[13] that you were using in performing the valuation?

[14] **A.** If I could take a step back, my relationship with the
[15] actual work product was as a manager. So I had very limited
[16] contact with Doral. At that time, when I arrived at Popular
[17] Securities, there was Francisco Bruguera, and at the same time
[18] joining me at Popular was Natalia Guzman, so those were the two
[19] employees that had the day-to-day contact with Doral. I only
[20] had contact with them, if I recall, three times, during the,
[21] during this period of time, from the time we did the work
[22] product for them.

[23] **THE COURT:** Keep your voice up because I'm not
[24] hearing. Did you say were there two other employees and so
[25] forth? Can you explain that again?

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[1] **THE WITNESS:** Yes. The team, when I got to Popular,
[2] there was four employees at Popular when I joined. One of
[3] them -- two of them did not work on the Doral IO valuation
[4] mandate. And two did. The two that did, Francisco Bruguera
[5] and Natalia Guzman, were the ones that worked in the investment
[6] banking area with me that were the personnel that talked to
[7] Doral, interacted with Doral, and had contact with them on a
[8] more frequent basis.

[9] **BY MR. STELLMACH:**

[10] **Q.** Could you explain for us, Mr. Kaufman, who it was at Doral
[11] that was the contact for Ms. Guzman and Mr. Bruguera in
[12] providing the criteria that they used in providing the
[13] calculations for the valuation?

[14] **A.** Again, you know, it's very, we don't, the office space was
[15] pretty small, so we knew each other's business, even though I
[16] was the manager. And the contact that I saw them having was
[17] with phone calls with Sam, Sammy Levis and with Sonia, which
[18] was Mr. Levis' secretary, I believe.

[19] **THE COURT:** Whose secretary?

[20] **THE WITNESS:** Mr. Levis, Sammy Levis' secretary.

[21] **THE COURT:** All right.

[22] **BY MR. STELLMACH:**

[23] **Q.** At any point, did anyone inside Popular tell you that the
[24] valuation that you were supervising was supposed to be an
[25] independent valuation?

[1] **A.** No.

[2] **Q.** When was the first time approximately that you learned that
[3] the valuation Popular was performing was being used as an
[4] independent valuation or being held out, I should say, to other
[5] people as an independent valuation?

[6] **A.** I remember clearly it was the time that they put out their
[7] 10K, somebody came into my office and said to me that they had
[8] filed a 10K, and I went to the computer and looked up the
[9] document that was available and saw that there was language in
[10] there that referenced the valuations that they were receiving
[11] as part of valuing that I don't portfolio. And I read the
[12] language, and I saw that they had referenced that there were
[13] these what they called external and internal. That was my
[14] recollection, and the words they used for both the internal and
[15] the external didn't seem to be the work product we were doing
[16] or didn't quite fit the fact pattern that I had been living, so
[17] more I felt we were reflected in the internal description and
[18] obviously not in the external.

[19] So I sent off an e-mail to Sammy Levis just asking him,
[20] that I saw this language and I just wanted to be sure that I
[21] understood it correctly and that we were the internal and that
[22] he was, even though I had agreed that the words he used to
[23] describe our work, that he would clarify that for us.

[24] **Q.** And what happened after you reached out to Mr. Levis; what
[25] did you learn?

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[1] A. Subsequently, two events. One, I, he responded, he
[2] responded by phone call. I guess I must not have been in the
[3] office or something. He responded to Natalia Guzman, who spoke
[4] to him. And she informed me that he had said we were the
[5] internal.

[6] THE COURT: He --

[7] THE WITNESS: She being Natalia Guzman, Ms. Guzman.

[8] THE COURT: Is that your secretary?

[9] THE WITNESS: No. That's the banker that worked in
[10] the investment banking, one of the two employees that worked in
[11] investment banking with us that had the relationship on the
[12] account.

[13] So she informed me that she received a call from
[14] Mr. Sammy Levis that said we were internal. Before I had
[15] received that confirmation, I had gone to lunch, I believe, and
[16] in the elevator bank I ran into another person that worked
[17] externally but worked closely with Doral, and I asked him. I
[18] was curious, that I had seen this language in the 10K and did
[19] he know what that referenced because it wasn't clear to me that
[20] it reflected accurately our role. He said he would go and
[21] check, so when we got back, I had got the confirmation later
[22] that afternoon from Natalia Guzman that Sammy had spoken to her
[23] and said we were the internal source.

[24] THE COURT: Sammy had spoken to her?

[25] THE WITNESS: Yes.

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[1] THE COURT: Okay.

[2] BY MR. STELLMACH:

[3] Q. Did there come a time when you learned that wasn't true?

[4] A. No, that he did speak to her.

[5] Q. No. Mr. Levis spoke to Ms. Guzman, but did there come a
[6] time when you learned that Popular's valuation had been held
[7] out to other people as an independent valuation?

[8] A. Later that afternoon as well, I got a call back from the
[9] gentleman that I had spoken to that had worked with Doral. He
[10] had checked with his sources at Doral, called me back, and said
[11] that he thought we were the independent, external source.

[12] Q. And could you remind us approximately when all this was
[13] taking place in connection with the filing of the 10K. What
[14] calendar year, what time period?

[15] A. Sorry. In March of 2005.

[16] MR. STELLMACH: Your Honor, I was about to go through
[17] the story in some detail. I don't know whether this would be a
[18] convenient point.

[19] THE COURT: It's a good time to take our break.
[20] (Recess)

[21] THE COURT: If it would be possible for you to speak a
[22] little louder, it would be good.

[23] Go ahead, please.

[24] MR. STELLMACH: Thank you, your Honor.

[25] Q. Mr. Kaufman, I'm going to go through your story from the

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[1] beginning, but before we do, I do want to jump back to the
[2] events of March 2005. And if you take a look at Government
[3] Exhibit 202, I'll ask if you recognize that exhibit, what's
[4] been marked for identification as 202.

[5] A. Okay.

[6] Q. Do you recognize it.

[7] A. Yes, I do.

[8] Q. How do you recognize it, sir?

[9] A. This is the e-mail that I had sent upon hearing about the
[10] language in the 10K filing in March of 2005 that I sent to
[11] Mr. Levis.

[12] MR. STELLMACH: Your Honor, the government offers
[13] Exhibit 202.

[14] THE COURT: Received.

[15] (Government's Exhibit 202 received in evidence)

[16] MR. STELLMACH: If we could see the exhibit on the
[17] screen.

[18] Q. We'll go through this in more detail later, Mr. Kaufman,
[19] but this is the e-mail on the bottom from yourself to
[20] Mr. Levis, dated March 17, 2005, is that correct?

[21] A. That's correct.

[22] Q. If we blow up the second full paragraph, beginning "on a
[23] separate note," you wrote that "we noticed that you include in
[24] Doral's 10K released yesterday the following language." And if
[25] you could, tell us what in that language caused concern for

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[1] you.

[2] A. As I said, you know, I had always believed that we were the
[3] internal, that we were, you know, providing a work product for
[4] Doral and working with them to come up as a tool, management
[5] tool for them with a valuation of this portfolio. So I read
[6] the language, it wasn't really, as I indicated earlier, there
[7] were two options here. You were the internal or you're one of
[8] the external. And as they referenced the external, it was
[9] obvious to me that we weren't that independent valuations
[10] because, one, I never believed we were an independent firm
[11] independently valuating their model, and it said, I think the
[12] language they used, "in which all economic and portfolio
[13] assumptions are determined by the preparer."

[14] To me, that was obviously not us, because that's not, that
[15] was not what we did. So I was left then, you know, that the
[16] other choice being that we were internal, and when I read the
[17] language, it just wasn't clear to me that -- I knew that we
[18] were definitely in this, not the external, but not the
[19] independent, but the internal, but the language of the internal
[20] that they used didn't seem that clear, and I just wanted to
[21] clarify with him that we, you know, we were in fact the
[22] internal. But it's the language he used.

[23] THE COURT: Were in fact the internal?

[24] THE WITNESS: Internal, yes.

[25] BY MR. STELLMACH:

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[1] Q. Because the 10K references three different valuations of
[2] the IOs, one being done internally and two others being done
[3] externally, in which all economic and portfolio assumptions are
[4] determined by the preparers. Is that right?
[5] A. That is correct. And we obviously, in my mind, you know, I
[6] know what we did for them, we were not independent valuation.
[7] We weren't those two independent valuations and those two
[8] external, because we did not, it was not -- all the economic
[9] and portfolio assumptions were not determined by us.
[10] Q. Could you just explain for us, Popular is obviously
[11] independent of Doral; it's not part of Doral. So the work
[12] Popular is doing could still be part of the internal valuation
[13] at Doral, was that your understanding?
[14] A. My understanding, exactly, was that. We were helping them
[15] in their internal valuation, in managing their portfolio and
[16] giving them a certain knowledge of what was there for them to
[17] make decisions about the portfolio.
[18] Q. And could you read that paragraph highlighted at the
[19] bottom, beginning, "Are we correct?"
[20] A. "Are we correct to assume that we are neither of the two
[21] external independent parties but a source you are using for
[22] your internal static cash flow model? The reason I presume
[23] that we are neither of the independent sources of valuation is
[24] because we rely (and so state in our letter/agreement) on
[25] portfolio and economic assumptions provided by Doral."

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[1] Q. If we could go to Mr. Levis' reply at the top of the page,
[2] he just wrote, "I will call you on this later," is that right?
[3] A. That is correct, which he did do.
[4] Q. And that led to a conversation between him and Ms. Guzman,
[5] who works for you?
[6] THE COURT: Before you go on, did you offer 202?
[7] MR. STELLMACH: I did, your Honor.
[8] THE COURT: Oh. Oh, I did receive it.
[9] BY MR. STELLMACH:
[10] Q. And that led to a conversation between Mr. Levis and
[11] Ms. Guzman, who works for you at Popular?
[12] A. Right. As I understand, when I got back, Ms. Natalia
[13] Guzman informed me that she had received a call from Mr. Mario
[14] Levis, Sammy, and that he confirmed that we were the internal
[15] source quoted, that was referenced in that 10K filing.
[16] Q. And after that conversation takes place, you learned from
[17] someone else that you are in fact being used as one of the
[18] independent valuations?
[19] A. I received a call back from a party I had run into on my
[20] way to lunch that I asked, and he called back and said that he
[21] had called people at Doral, I don't know who, and said I
[22] believe that they think you are the independent valuation
[23] party.
[24] Q. All right. And so what I want to do now, Mr. Kaufman, is
[25] step back to the beginning, when you first joined Popular, in

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[1] September of 2003, and begin working on this project. Now,
[2] when you started at Popular, in 2003, who were you replacing?
[3] A. I arrived in September of 2003, and the previous person
[4] that occupied the seat that I was hired to fill was Mr. Carlos
[5] Ortiz, also known as Juany Ortiz.
[6] Q. Did you know Mr. Ortiz?
[7] A. Yes, I did.
[8] Q. And what was your understanding of his relationship with
[9] the defendant?
[10] A. I understood that they had a close relationship.
[11] Q. Did they socialize together?
[12] A. I believe so, yes.
[13] Q. Did you know whether the defendant had been the best man at
[14] Mr. Ortiz's wedding?
[15] A. I did not know that.
[16] Q. How soon after you started at Popular did you learn that
[17] Popular was performing a valuation of Doral's IOs?
[18] THE COURT: I missed something. Did you replace
[19] Ortiz? Did he leave? I didn't understand.
[20] THE WITNESS: When I arrived, he had left
[21] approximately in June, July period. The time that I, between
[22] that, his leaving and my arriving, the president of Popular
[23] Securities, Ken McGrath, oversaw the investment banking area
[24] and then when I arrived in September, I took over the reins.
[25] BY MR. STELLMACH:

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[1] Q. So you didn't overlap with Mr. Ortiz; once you started he
[2] was already gone?
[3] A. Yes.
[4] Q. And how soon after you started at Popular did you learn
[5] about this IO valuation project?
[6] A. Within hours or days. I was, you know, brought up to speed
[7] on the work we were doing. When I started work, and I think
[8] the, within probably the first day or two, I was visited by one
[9] of my colleagues who had some concerns about the mandate and
[10] wanted to talk to me about it.
[11] Q. How did you first learn; who at Popular first told you
[12] about the valuation project?
[13] A. I believe that we had a few different things going on, a
[14] few different deals going on, so it was one of a list of
[15] ongoing work product that we had. And I was, I believe,
[16] brought up to speed of what was on by each of the bankers who
[17] were handling the matters that related to them. At that time,
[18] Francisco Bruguera was handling the IO valuation.
[19] Q. And when you say handling the valuation, was Mr. Bruguera
[20] actually performing the calculations to execute the valuation?
[21] A. He was.
[22] Q. And did that continue after you started at Popular?
[23] A. It did.
[24] Q. So at any point during your tenure at Popular, are you the
[25] person at Popular who is actually crunching the numbers and

Exhibit M

In The Matter Of:

*UNITED STATES OF AMERICA v.
MARIO S. LEVIS A/K/A SAMMY LEVIS*

*VOLUME 13
April 14, 2010*

*TRIAL
SOUTHERN DISTRICT REPORTERS
500 PEARL STREET
NEW YORK., NY 10007
212-805-0300*

Original File 04EJLEVF.txt, Pages 1912-2080 (169)

Word Index included with this Min-U-Script®

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(1) colleagues and your awareness of what was taking place at your
(2) firm during that period of time?
(3) A. Correct.
(4) Q. So it's not a recollection of the conference call itself?
(5) A. Exactly.
(6) Q. Did you remain involved in the project going forward from
(7) September of 2003 into the future?
(8) A. I was, yes.
(9) Q. Did there come a time when you became more responsible for
(10) the project yourself?
(11) A. Yes. When Francisco left, I became responsible for it.
(12) Q. And Francisco is Francisco Brugueras?
(13) A. Correct.
(14) Q. And about what time did he leave Popular Securities?
(15) A. He left at some point in the summer of 2004.
(16) Q. And where did he go?
(17) A. He went to do his MBA at University of Chicago.
(18) Q. So he went off to business school?
(19) A. Correct.
(20) Q. Did you essentially take his role within the valuation work
(21) at that time?
(22) A. Correct.
(23) Q. And you had been doing, working on the project in a more
(24) junior role over the course of the past year, is that right?
(25) A. Correct, yes.

(1) Q. Not from someone else at Doral?
(2) A. Yeah.
(3) Q. Were they ever answering, to your knowledge, based on your
(4) communications with them, were they ever able to provide you
(5) with information based on their own personal knowledge?
(6) A. None whatsoever. It was just all information that they
(7) were giving to us from someone else.
(8) Q. And if I understand you, the someone else they mentioned to
(9) you was Sammy Levis?
(10) A. Correct.
(11) Q. Did you have any direct dealings with David Levis?
(12) A. Only in March of 2005, when Greg and I went to meet with
(13) David Levis and Sammy Levis. That was my only interaction with
(14) him.
(15) Q. Right. Can you turn your attention to Government Exhibit
(16) 171, which should be in your binder?
(17) A. Yes.
(18) Q. It should be the next document.
(19) MR. BRAUN: And this is already in evidence, your
(20) Honor.
(21) Q. Ms. Guzman, when you became more responsible for this
(22) project regarding the IO valuation, did you seek to obtain
(23) additional information regarding these caps that you understood
(24) had been described the previous September?
(25) A. Yes, we did.

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(1) Q. As you became more responsible for the project and stepped
(2) in for Mr. Brugueras, did you have direct dealings with anybody
(3) from Doral Financial in connection with this work?
(4) A. After September? Or 2004 or before?
(5) Q. From the period of time in which you became more
(6) responsible.
(7) A. From that period of time on, I had interactions with Sammy
(8) Levis and Sonia Arroyo and Lorna, I believe. Soto is her last
(9) name. Secretaries of Sammy Levis.
(10) Q. All right. Both Sonia Arroyo and Lorna Soto were
(11) secretaries at Doral?
(12) A. That was my understanding, yes.
(13) Q. And your understanding was that they worked for Sammy
(14) Levis?
(15) A. Correct.
(16) Q. During the course of your conversations with Ms. Arroyo and
(17) Ms. Soto, did they indicate to you whether or not they were
(18) providing you with information on anyone else's behalf?
(19) A. Not from my understanding. From what I recall, it was
(20) always, they said that it came from Sammy.
(21) Q. All right. That was my question. I just phrased it very
(22) poorly.
(23) A. Oh, I'm sorry. Yes. Just from Sammy. It was always
(24) information that they were relaying, right, from Sammy, but not
(25) from somebody else.

(1) Q. And is this e-mail a part of that effort?
(2) A. Correct.
(3) Q. Can you read your message to Sammy in this e-mail, dated
(4) Tuesday, September 14, 2004?
(5) A. "Sammy, as per our conference call held September 19, 2003,
(6) with Gregory Kaufman, Francisco Brugueras, Jose Blasini and
(7) myself, we have applied an average cap rate of 3.40 percent to
(8) most pools of inverse IOs, in specific to those in group 3. We
(9) would like to confirm the method used to hedge interest rate
(10) risk. In particular, please explain the structure of the cap
(11) rate and any other derivative instruments used, as well as the
(12) pools that each instrument is hedging.
(13) "Should you have any questions, please contact me at the
(14) number below. Thank you. Natalia."
(15) Q. What was your reason for seeking this information from
(16) Sammy Levis?
(17) A. We had internal discussions that the cap rate sounded low,
(18) and we --
(19) THE COURT: You had internal discussions about the cap
(20) rate, and then what did you say?
(21) THE WITNESS: That it sounded low for industry
(22) purposes, and we wanted to have more details about it.
(23) BY MR. BRAUN:
(24) Q. And this cap rate, let me take you a step back, what did
(25) you understand was actually being capped at 3.4 percent?

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[1] A. The 3.4 percent was effectively capping or, the cap was
[2] capping the floating interest that Doral had to pay to the
[3] buyers of the loans. Right?
[4] Q. Okay.
[5] A. So the floating, the floater investors.
[6] Q. And it was that level of 3.4 percent, if I understand you,
[7] that sounded low?
[8] A. Correct.
[9] Q. You mentioned group 3 in your e-mail. Did that group stand
[10] out in any way?
[11] A. Yes, that was the largest group of the portfolio.
[12] Q. And as far as the composition of group 3, what
[13] characteristics did it have as far as the composition of fixed
[14] as opposed to floating rate IOs?
[15] A. I believe it was entirely floating.
[16] Q. Could it have been a couple of fixed portions to it?
[17] A. Maybe, but something like that.
[18] Q. This information regarding the caps and any other
[19] derivative instruments, did you consider it to be important?
[20] A. Absolutely.
[21] Q. Why was it important to you?
[22] A. Because it was effectively, I mean, the cap at 3.4 as Doral
[23] had disclosed, was effectively fixing their, or guaranteeing
[24] their excess spread in, I mean, their IO income, right, on the
[25] portfolio.

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[1] Q. Was it having a significant impact on the valuation numbers
[2] that you were producing at Popular Securities?
[3] A. Yes. At that time, basically, it was almost capping
[4] entirely, so from, if we would run the cash flows, like almost
[5] like from day 1, from the day we did the valuation, the cap
[6] took, took effect, right, so the forward curve, increases in
[7] the forward curve weren't shown, weren't taking any effect in
[8] the portfolio's value.
[9] Q. Because you were hitting the cap so quickly?
[10] A. Right.
[11] Q. Do you recall receiving a response to the question that you
[12] posed in this September 14 e-mail?
[13] A. Can you repeat that again?
[14] Q. Yes. Do you recall receiving any information in response
[15] to the e-mail that we just looked at dated September 14, 2004?
[16] A. Yes, we did.
[17] Q. Can you turn to the next document in your binder? Do you
[18] recognize this document, Ms. Guzman?
[19] A. I do.
[20] Q. What do you recognize it as?
[21] A. These are my notes from the response from Doral. I would
[22] imagine probably I spoke to Sonia or Sammy, and this is a
[23] response to the e-mail that I sent.
[24] Q. And do you recall whether it was Sonia Arroyo, the
[25] secretary, or Mr. Levis himself?

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[1] A. I don't recall specifically who did I speak with.
[2] Q. Was it one of those two people?
[3] A. I would imagine so, yeah, because those are the two people
[4] that I spoke to.
[5] Q. Can you explain what information is reflected here in your
[6] handwritten notes, dated September 14, 2004?
[7] THE COURT: I think this is not yet in evidence, is
[8] it?
[9] MR. BRAUN: I apologize, your Honor. We offer 170,
[10] Government Exhibit 170.
[11] THE COURT: Received.
[12] (Government's Exhibit 170 received in evidence)
[13] MR. BRAUN: Thank you.
[14] A. You want me to read it?
[15] Q. If you could either read it or perhaps more helpfully
[16] explain it to us.
[17] A. Okay, yeah. So basically, they're just telling us that the
[18] average cap rate for groups 1 through 4 was 3.4, except, of
[19] course, for the fixed pools that were in those groups, that it
[20] was a five-year cap, and that they also had European put
[21] options that locked in also the average cap rate of 3.4. That
[22] says group No. 3, all five-year caps. Then it says five-year
[23] caps, three and three-eighths, so I think that they were
[24] disclosing that it was three and three-eighths, not 3.4, just
[25] to be more specific. Mature in 2007 and 2008 and are

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[1] renewable. This is information that they're giving us.
[2] Q. Okay. To be more precise, three and three-eighths, how
[3] does that compare to 3.4?
[4] A. It's just, point three and three-eighths means 3.375, so
[5] it's a difference between 3.4 and 3.75, which is .025.
[6] Q. And you understood that to be a more precise number as
[7] opposed to the 3.4?
[8] A. Correct.
[9] Q. Do you recall whether or not you had any conversations
[10] relating to the subject with Ms. Arroyo or Mr. Levis during
[11] this period of time? Could there have been other
[12] communications on the same subject?
[13] A. Yes, there were.
[14] THE COURT: I'm sorry. I didn't hear.
[15] THE WITNESS: Yes, there were other communications. I
[16] believe there's another e-mail that I sent out.
[17] BY MR. BRAUN:
[18] Q. Can you turn your attention to Government Exhibit 173,
[19] which is already in evidence?
[20] A. Mm-hmm. I have it here.
[21] Q. And can you read your message to Sammy Levis here on
[22] September 17, a few days later?
[23] THE COURT: What's the exhibit number?
[24] MR. BRAUN: This is 173, your Honor. It was admitted
[25] yesterday.

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(11) **THE COURT:** All right.
(12) What's your question now?
(13) **MR. BRAUN:** I was asking Ms. Guzman if she could read
(14) the short e-mail here to Sammy Levis.
(15) **THE COURT:** Okay.
(16) A. "Sammy, before finalizing our results for the IO valuation,
(17) we would like to clarify the definition of the inverse IO cap."
(18) Q. Can I stop you there for a moment. Inverse IO, can you
(19) explain that?
(20) A. Yeah. That's basically, the inverse IO is what they are
(21) keeping in their books. So the floater portion, right, is
(22) what's being sold to the investors, and the remaining portion
(23) of the ones that are variable, is what they keep.
(24) Q. So the kind of floating rate IO Doral had also referred to
(25) as an inverse IO?
(1) A. Correct.
(2) Q. Okay. Please continue.
(3) A. "We are unclear about whether the cap rate is a cap on the
(4) LIBOR rate alone, or a cap on the gross funding cost (LIBOR
(5) plus spread) payable to investors."
(6) Q. When you refer to the gross funding cost, is that another
(7) way of referring to the pass-through rate that Doral is going
(8) to provide to the banks that buy these loans?
(9) A. Correct.
(10) Q. Please continue.

(11) cap of 3.375 is still above, right, the 2 percent of the LIBOR.
(12) So then they would pay the investor the 2 percent plus the 1.5.
(13) If the cap is not only capping the LIBOR, but it's capping the
(14) LIBOR plus the spread, then it means that they are in effect
(15) just paying 3.375 to the investor. And not 3.5.
(16) **BY MR. BRAUN:**
(17) Q. Ms. Guzman, do you recall receiving a response to the
(18) question you posed regarding whether the cap was a cap on how
(19) high LIBOR went or whether or not it was actually capping the
(20) full pass-through rate consisting of LIBOR plus whatever spread
(21) the investor or the bank that bought these loans was going to
(22) receive?
(23) A. Yes. They told us it was capping the LIBOR plus the
(24) spread.
(25) Q. Can you now turn your attention to Government Exhibit 175
(1) that's been marked for identification?
(2) A. I have it in front of me.
(3) Q. Do you recognize the document?
(4) A. I do.
(5) Q. Are these your notes, Ms. Guzman?
(6) A. Yes, it's my handwriting, and the left is Marvin Diaz's
(7) handwriting, who is the analyst at that time.
(8) Q. I don't think you've mentioned Mr. Diaz before. Can you
(9) explain who he was and what role he was playing at Popular
(10) Securities?

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(11) A. "For instance, given a LIBOR rate of 3.50 percent and a
(12) spread of 150 basis points, which means 1.5 percent, how much
(13) would you pay the floating rate investor? Would you pay 3.375
(14) percent plus the spread or just 3.375 percent. In addition --"
(15) Q. Let me skip that next sentence.
(16) A. Okay.
(17) Q. So what, in essence, is the question here you're posing to
(18) Sammy Levis?
(19) A. So, in essence, what we're asking is whether the cap of
(20) 3.375 is capping just the LIBOR or capping the LIBOR plus the
(21) spread.
(22) Q. So the entire pass-through rate or just the LIBOR?
(23) A. Exactly. So to the extent that, right, LIBOR rate was at 2
(24) percent and the spread was 1.5 -- yeah, whether they, whether
(25) they had to pay to the investor the 2 percent, right, plus the
(1) 1.5 because the 2 percent, in the case that the cap was just
(2) capping the LIBOR, they would be in effect then paying 3.5 to
(3) the investor. To the extent that the cap was capping the LIBOR
(4) plus the spread, then they wouldn't be paying 350, they would
(5) be paying 3.375.
(6) Q. Do you recall --
(7) **THE COURT:** I don't understand the last answer. In
(8) other words, say that again.
(9) **THE WITNESS:** Okay. So if the cap is capping just
(10) LIBOR and LIBOR is at 2 percent and the spread is at 1.5, the

(11) A. So after Francisco Bruguera left, we hired Mr. Diaz. He
(12) came straight from undergraduate studies at UPenn and started
(13) working that summer of 2004, so he, he and I worked on the
(14) Doral IO valuation going forward.
(15) **MR. BRAUN:** Your Honor, the government offers Exhibit
(16) 175 into evidence.
(17) **THE COURT:** Received.
(18) (Government's Exhibit 175 received in evidence)
(19) **BY MR. BRAUN:**
(20) Q. Turning to the top portion of this handwritten note,
(21) Ms. Guzman, going down to the figure 3.375 percent, can you
(22) explain what information you're receiving here that's reflected
(23) in your notes?
(24) A. It says the cap equals LIBOR plus the spread, 3.375. As
(25) confirmed.
(1) Q. And what part of this do you recognize as Mr. Diaz's
(2) handwriting?
(3) A. The part on the left that says, it says in it in Spanish,
(4) but it means conversation with Sonia regarding e-mail cap rate.
(5) That, that's his handwriting. The rest is mine.
(6) Q. Can you turn your attention to the next document in your
(7) binder, which is marked for identification as Government
(8) Exhibit 176?
(9) A. Yes, I have it in front of me.
(10) Q. Do you recognize this set of notes?

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[1] A. I do.
[2] Q. Do they reflect another communication you had with folks
[3] over at Doral?
[4] A. Yes.
[5] MR. BRAUN: Your Honor, the government offers Exhibit
[6] 176.
[7] THE COURT: Received.
[8] (Government's Exhibit 176 received in evidence)
[9] BY MR. BRAUN:
[10] Q. Ms. Guzman, the set of notes appears to be dated September
[11] 17, 2004, correct?
[12] A. Correct.
[13] Q. And the top line, what does that mean to you, Sonia,
[14] conversation with Sammy?
[15] A. I'm not sure if it means that I first spoke to Sonia and I
[16] then spoke to Sammy, or if it means I'm speaking to Sonia and
[17] it's regarding what Sammy told her. Could be either of the
[18] two.
[19] Q. There's some information at the top with the two groups,
[20] No. 2 and 8, and a notation regarding the CPR. Can you first
[21] explain to us what CPR refers to?
[22] A. CPR is constant prepayment rate. And it refers to the
[23] percentage, so let's say CPR in one year is 6 percent. It
[24] refers to the percentage of the unscheduled principal, of the
[25] outstanding principal, right, that was prepaid during that

[1] A. Yeah, we always did that.
[2] Q. And was it your practice also to obtain Doral's approval
[3] before finalizing it and sending it to them in a letter form?
[4] A. Yes, in a way.
[5] Q. Now, can you turn your attention to the next document in
[6] your binder, which is Government Exhibit 177?
[7] MR. BRAUN: It's already been admitted, your Honor.
[8] A. I have it in front of me.
[9] MR. BRAUN: Can we blow up what's already been
[10] highlighted at the bottom of that page?
[11] Q. Do you see the highlighted language on the screen,
[12] Ms. Guzman?
[13] A. Yes.
[14] Q. Can you read that language at the bottom of this September
[15] 17 letter?
[16] A. "We have relied on representations by the company that 97
[17] percent of its inverse IO portfolio has a gross funding cost
[18] (LIBOR plus spread) capped at three and three-eighths percent,
[19] and the other 3 percent of its inverse IOs are hedged through
[20] European put options. This hedging activity protects the
[21] current pass-through interest rate and excess interest spread
[22] in its floating IOs."
[23] Q. Is this information consistent with what you had been told
[24] in the conversations with Sammy Levis and Sonia Arroyo that
[25] you've described in your testimony this morning and that's

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[1] year. So if the CPR is 6 percent, it means that 6 percent of
[2] the principal was prepaid through that year.
[3] Q. And did you provide information regarding the prepayment
[4] rates that you had determined in information that you gave to
[5] Mr. Levis prior to the time your valuation work was finalized?
[6] A. Can you repeat that again?
[7] Q. Yes. Prior to the time that you finalized an evaluation
[8] that you were working on for a particular quarter, say, was it
[9] your practice to provide Mr. Levis over at Doral with
[10] information regarding the numbers that you were coming up with?
[11] A. Yes. We would send them a draft of our valuation.
[12] Q. And did the draft of your valuation often include the
[13] prepayment rates or CPR numbers that you had determined during
[14] the course of your work?
[15] A. Yes.
[16] Q. And did you sometimes receive feedback from Mr. Levis or
[17] his secretaries regarding those numbers?
[18] A. Yes.
[19] Q. Where it says he approved the draft, is that the draft
[20] valuation table that you just described?
[21] A. I would imagine so, yes.
[22] Q. And then it says draft was finalized and sent to Doral?
[23] A. Correct, yes.
[24] Q. Was it your practice to send over the table reflecting your
[25] numbers in advance of the time you finalized it?

[1] reflected in your notes?
[2] A. Yes, it is.
[3] Q. Do you recall sending this September 17, 2004, letter to
[4] Doral?
[5] A. Yes.
[6] Q. After you sent the letter, what took place?
[7] A. Sammy called, and he sent the fax over with the letter from
[8] September 2003.
[9] Q. And when Sammy called, who took the call at Popular
[10] Securities?
[11] A. I did.
[12] Q. And do you recall the conversation that you had with
[13] Mr. Levis on that occasion?
[14] A. I do.
[15] Q. Can you describe the conversation for us, Ms. Guzman?
[16] THE COURT: Can we just say, the date of this draft is
[17] what?
[18] MR. BRAUN: It is September 17, 2004, your Honor.
[19] That's Government Exhibit 177.
[20] THE COURT: All right. And now the conversation,
[21] Mr. Levis called you?
[22] THE WITNESS: Yes.
[23] THE COURT: The question is? Let me hear the question
[24] again. I interrupted.
[25] MR. BRAUN: She indicated, your Honor, that Ms. Guzman